

FUTURE OF INDEPENDENT OIL AND GAS EXPLOR- ERS/PRODUCERS: MARKET TRENDS AND TAX REFORM

HEARINGS

BEFORE THE

SUBCOMMITTEE ON ENERGY, ENVIRONMENT,
AND SAFETY ISSUES AFFECTING
SMALL BUSINESS

OF THE

COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES

NINETY-NINTH CONGRESS

SECOND SESSION

ODESSA, TX, APRIL 1; AND ABILENE, TX, APRIL 2, 1986

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FUTURE OF INDEPENDENT OIL AND GAS EXPLORERS/PRODUCERS: MARKET TRENDS AND TAX REFORM

TUESDAY, APRIL 1, 1986

**HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON ENERGY, ENVIRONMENT, AND
SAFETY ISSUES AFFECTING SMALL BUSINESS,
COMMITTEE ON SMALL BUSINESS,
Odessa, TX.**

The subcommittee met, pursuant to notice, at 9:05 a.m., in city council room, City Hall, 411 West 8th Street, Odessa, TX, Hon. Charles W. Stenholm (chairman of the subcommittee) presiding.

Mr. STENHOLM. This meeting of the Subcommittee on Energy, Environment, and Safety Issues Affecting Small Business, will now come to order. My name is Charlie Stenholm and in addition to representing the neighboring district, the 17th District of Texas, I have the privilege of chairing this subcommittee. Before I proceed further with my opening statement, I would like to turn the floor over to my friend, colleague, and member of this subcommittee, the Honorable Larry Combest.

OPENING STATEMENT OF HON. LARRY COMBEST, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. COMBEST. Mr. Chairman, thank you. I appreciate your agreeing to hold this very important meeting in my district. Last November, I requested that Congressman Stenholm hold a hearing of the Small Business Subcommittee on Energy, Environment, and Safety in the Odessa area. I did so because of my increasing concern for the independent oil and gas producer, in light of developments over the past several years, which have led to a severe situation of economic hardship, not only for the producers but for the entire Permian Basin economy.

With oil market future deliveries for May opening at \$9.90 this morning, with the Permian Basin rig count down 46 percent from this time last year, and with an unemployment rate expected to exceed an 11-year record in March, I believe it is evident that this has become a matter of critical proportion. Bearing in mind that the major portion of the energy exploration and development activity is conducted by small, independent businessmen, the ramifications of the continued decline in the industry for the Permian Basin region is national in scope.

For many years the oil and gas industry has borne the brunt of a number of significant negative changes in tax policy. These

changes have fallen especially on the small, independent oil and gas producer. The distinction created by negative tax treatment is only magnified by the House-passed Tax Bill, which I strongly oppose and believe will devastate the energy industry. These proposals could adversely impact outside investment capital, and unless modifications are made, funds will be diverted away from petroleum development exploration into less risky, but less essential, economic activity.

Recent surveys of independent producers' have indicated declines in exploratory drilling by 75 percent over the past several months. These projected declines are from a level of activity, which is already at least 50 percent below that required to maintain production at its present level, much less to meet the future increases in consumption due to growth of the economy.

These points lead me to a matter of great concern. As a result of this inability to attract capital for exploration, an environment which harbors an over-dependence on foreign oil is perpetuated. Domestic American oil must always be available for the Nation's defense.

Unless oil is produced continuously, and aggressive exploration continues to replace dwindling American reserves with new discoveries, the U.S. oil industry will be strangled to undermanned ineffectiveness. We will be unable to provide necessary supplies of oil, when they could be most urgently needed for the protection of our citizens, and the ultimate future of our country. The best prophet of the future is the past, and to allow ourselves to be placed once again in a position of vulnerability to foreign countries for our national energy supply, is intolerable.

To insure that the goal of sustaining incentives for continued operation of current production, and the progressive exploration and development of future reserves, we must develop a comprehensive national energy policy. It is essential in the long term, best interest of our Nation that we preserve a strong energy-producing sector. A policy which provides the opportunity for the oil industry, particularly independent producers, to attract capital and incentives for continued exploration, will allow us to achieve a level of energy independence and the industries ability to attain these ends.

I am original cosponsor of the Emergency Energy Act of 1986, which I believe will foster industry recovery, and send a strong message both to the American people and the world that we remain committed to the principle of energy independence and freedom.

I appreciate the members of the panel taking the time to provide us information relating to the impact of the currently depressed industry on the local business and economy of the Permian Basin area, for you are truly the experts. This input will be vital as the Congress works toward enacting measures that will best serve independent oil and gas producers of the Nation.

Mr. Chairman, I appreciate your being here and I appreciate your time and your attention.

OPENING STATEMENT OF CHAIRMAN STENHOLM

Mr. STENHOLM. Let me begin by extending a warm welcome to the witnesses and others in attendance here today. We appreciate very much your interest in the subject at hand, the future of independent oil and gas producers, market trends and tax reform. In addition, I would like to express the subcommittee's appreciation to Mr. John Harrison, city manager for the city of Odessa, for making the city council chambers available to us today.

I should also add that the subcommittee is holding an identical hearing tomorrow in Abilene and I appreciate my colleague Larry coming to Abilene for this hearing as well.

U.S. domestic oil and gas explorers and producers are suffering from a severe depression, the effects of which are immediately devastating to the State of Texas and potentially catastrophic for the Nation's economic security. Independent producers who historically drill 86 percent of the development wells, and 90 percent of the wildcat wells, have all but abandoned the search for oil in the United States. If this situation continues, U.S. proven reserves will shrink as we fail to replace our reserves with new discoveries.

The United States currently imports one-third of its crude oil supply and depends on its domestic oil and gas industry for the remaining two-thirds. Coupling the projected production decline with the expected increase in imports, imports may soon total 53 percent of our consumption rather than the present 36 percent. Based upon our experience of the 1970's, this scenario is cause for deep alarm for everyone concerned with our national security, the risk to our economy, and the long term well-being of our consumers. The negative impact of low oil prices on U.S. crude oil production will have a greatly accelerated effect as the perception of permanence sets in.

The price slide of the past 90 days is not the result of supply and demand market economics. It results from punitive, monopolistic actions designed to undercut high cost producers, by the world's single most dominant producer. Saudi Arabia has embarked on a course to recapture what it perceives to be its share of the world oil market. Over the past 6 years, the Saudis have seen their share of free world production decline from 19 percent to 6 percent. At this time there are legitimate reasons to justify the creation of a fee on all imports, apart from the need for additional revenue to reduce the massive budget deficit.

The United States cannot avoid an increasing reliance on dependable petroleum imports unless major steps are taken to increase domestic exploration and development of oil and gas, and to extend the lives of marginal oil and gas producing properties. The drive within Congress to enact tax reform legislation remains alive. I oppose the House version of such legislation because of the punitive energy tax provisions contained in the bill, H.R. 3838. The initial Senate effort as introduced by the chairman of the Finance Committee, would retain present tax law for domestic production of oil and gas. These circumstances leave the door open for a possible House/Senate compromise giving us something between the House bill and existing treatment of intangible drilling costs and

percentage depletion, or the possibility of no bill at all. This still remains my personal preference.

The problems within the domestic oil and gas industry are many and varied. The subcommittee wants to build a hearing record to take back to Washington for consideration and reference as the Congress and the administration prepare and implement policies to address the current crisis, as well as to develop a long-term energy policy for this Nation. This subcommittee does not have, and I repeat, does not have primary jurisdiction in the tax area or in the overall policymaking area as far as oil and gas are concerned. We have jurisdiction in the area of small business.

We held hearings last year in Los Angeles and Houston in order to look at some of the problems of offshore oil production and particularly the results of the moratorium that has been in place in the California region for the past several years. As a result of these hearings, we were able to build a record which was used during deliberations on the future of the moratorium. We intend to build a record to ascertain the future of the independent oil and gas industry, given the current price situation. We believe this record can be utilized in a very positive and helpful way as the Congress and administration attempt to develop policies to address the problems that are facing the oil and gas industry today.

We welcome those who will testify today. I will call the first panel to the table, Mr. James Williams, Mr. Buzz Hurt, Mr. Sam Holloman, Mr. Ron Fancher and Mr. Charles Perry. If you all would take your places at the table, we will hear from each and every one of you. If you have a long statement, we would appreciate very much your summarization of it. Try to keep your testimony as close to 10 minutes as you can. We do not have a large witness list today so we can be somewhat flexible. Both your prepared and oral statements will be made a part of the record.

At the end of each panel, Mr. Combust and I will have some questions for you. Gentlemen, we welcome you and we will first hear from Mr. James L. Williams, of Texas Business Forecasts, Midland, TX. Mr. Williams.

TESTIMONY OF JAMES L. WILLIAMS, TEXAS BUSINESS FORECASTS, MIDLAND, TX

Mr. WILLIAMS. Thank you, Mr. Chairman. I want to thank you and the members of the subcommittee for giving us the opportunity to testify before you today. My name is James L. Williams, I live in Midland, TX and I am a principal in Texas Business Forecasts, a local consulting firm which supplies economic and financial consulting services primarily to people in the Permian Basin.

The purpose of my testimony is to try to assist you in analyzing and assessing the impact of falling crude prices and various energy policies on citizens and businesses in west Texas and to discuss a few domestic and national security ramifications of prices and policy.

An analysis of crude oil prices on employment can be an effective tool in understanding the energy industry. The geologic region known as the Permian Basin is the source of a significant portion of the production of oil and gas in the United States and almost all

of the economic activity in the Permian Basin is directly or indirectly related to the oil and gas industries. For this reason, the study of Permian Basin economy can yield valuable insight into the effects of crude oil price changes and energy policy on the industry as a whole and upon regional economies with significant employment related to exploration and production of oil and gas.

The Texas cities of Midland and Odessa are representative of the Permian Basin economy and how we use them to illustrate the impact of crude prices on various governmental policies.

In 1982, virtually 100 percent of the category known as mining employment in the employment statistics in Midland and Odessa was related to petroleum or natural gas exploration production. Approximately 75 percent of the manufacturing employment was energy related. In fact actually somewhat more than that because of the large petro chemical in the area. Employment in the mining and manufacturing industries is heavily dependent upon domestic prices for oil and gas. Tables I-IV track crude oil prices and employment in both cities.

In response to the Arab oil embargo, international prices for crude quadrupled in 1973. From 1973 to 1978, prices were relatively stable and the Iranian revolution caused another rapid increase in prices during 1979 and 1980. International prices rose to 250 percent of the 1978 price by the end of 1980. Throughout this period, domestic production was subject to price control. Because of price controls, domestic prices were significantly lower than the international prices. And domestic exploration production of course is dependent upon prices received by U.S. producers. For this reason, domestic crude prices will be used to analyze the impact of price changes on the local industry and employment.

In 1975 domestic crude prices averaged \$7.18 per barrel. By 1978 they had been allowed to increase to \$10.61 a barrel and from that year to 1981, prices increased to \$37 a barrel, 3.5 times the price of 1978. This rapid increase was brought about by the increase in international prices and the deregulation of domestic crude oil prices. In 1975, oil and gas employment, that is mining employment in Midland and Odessa, averaged 7,190 people and 6,320 respectively. By 1978, the number of oil and gas employees in the respective cities had increased to 9,100 and 7,490. The 48-percent increase in domestic crude prices caused a 23-percent increase in the number of jobs in this sector.

Manufacturing employment in Midland and Odessa in 1975 was 2,230 and 5,500 respectively. By 1978, manufacturing employment had increased 34 percent to 3,860 and 6,530 in the respective cities.

In response to the rapid increase in crude prices from 1979 to early 1981, employment in both oil and gas manufacturing grew at tremendous rates. Because of the high rate of growth and the limitations on housing, offices and manufacturing facilities, the growth continued for some time after domestic prices peaked at \$37 a barrel in March 1981. Mining employment in Odessa peaked at 10,000 in January 1982. Manufacturing employment topped out in the same month at 10,100. Mining and manufacturing employment in the Odessa MSA had increased 34 and 84 percent respectively over the 1978 averages. Midland showed a similar pattern with mining employment peaking at 14,700 in February 1982 with an in-

crease of 62 percent over the 1978 average and manufacturing increasing 31 percent to peak at 5,000 in September 1981.

In response to the 27-percent decrease in domestic prices from \$37 in March 1981 to below \$27 a barrel at the end of 1985, employment in manufacturing and mining showed a rapid decline. In Midland, manufacturing dropped 27 percent and mining employment decreased 21 percent. Odessa showed a 10-percent decline in mining employment and manufacturing employment in Odessa dropped 49 percent to 5,280 in 1985. In short, much of the industry infrastructure which was built in response to the rise in crude oil prices has already been lost. We have lost essentially 50 percent of our manufacturing business at least as measured by employment in the local area since 1982.

Manufacturing and oil and gas combine to form the base for economic activity in Midland and Odessa. The effects of changes in this base trickle through to other sectors of the economy. Some sectors take over a year to react to changes in the economic base which represents approximately 30 percent of the total wage and salary employment in the area. From 1975 to 1981, crude oil prices increased 378 percent. Assuming the effect on Midland and Odessa, employment lags prices by about a year. This compares to a 170-percent increase in employment from 1975 to 1982. During that period for each 10-percent increase in crude prices, there was a corresponding 4.5-percent increase in employment. Midland-Odessa employment rose from an average of 68,000 in 1975 to 116,000 in 1982. From 1981 to 1984, crude prices dropped 17 percent and during the corresponding 1982-85 period employment declined 12.5 percent.

The downside experienced a 7.3-percent drop in employment for each 10-percent decline in the price of crude oil. If one just makes the conservative assumption that for a 10-percent drop in crude prices in the future there will be a 5-percent longrun decline in employment in the area and if crude prices average \$15 per barrel and we heard that they are below \$10 this morning, but if they just averaged \$15 a barrel for 1986, employment in the area will fall from a current level of 100,000 to below 85,000 by the end of 1987 and it is entirely possible that that number could be 25,000. We are talking about losing 25 percent of the existing jobs in the Permian Basin economy within a 2-year period.

The stress on the local economy of a further decline in employment of that magnitude could be beyond measure. Since 1981 we've experience three bank failures just in Midland and Odessa and numerous other failures in the Permian Basin and one of those is one of the largest independent banks in Texas. Housing prices have declined over 20 percent. Few people who purchased a home in 1982 are able to sell it for the balance due on their mortgage. If you purchased a home for \$100,000, you would be very fortunate to get \$80,000 on the market. A typical person who purchased a home with 5- or 10-percent down would actually have to come up with \$10,000 to \$15,000 just to sell it.

Residential and commercial rental property does not generate enough income to meet cashflow requirements. There are more filings for bankruptcy in a month than there were for the entire year of 1979.

More important than the impact on the local economy are the implications of energy price decline for the future of the industry as a whole. The latest count of rotary rigs running in the United States is 1,063, down 73 percent from the average of 3,970 in 1981. Rig utilization in the Permian Basin as well as the United States is below 25 percent of the current rate fleet. This means domestic oil and gas reserves are not being replaced as fast as they're being depleted. The implication for U.S. energy balance of such a low rate are clear. Within 3 to 5 years, perhaps earlier at current price levels, there will be a significant drop in production. This drop in domestic production will be caused by failure to replace reserves and the inability of many of the wells, which are currently in production, to generate positive cashflow. Many stripper wells have already been abandoned.

The scenario that the United States and the world faces is the mirror image of our experience in the 1973-81 period.

Since the beginning of this decade, two major forces have worked together to force down the price of petroleum. The rapid increases in crude oil prices as a result of the Arab oil embargo in 1973 and the Iranian revolution was to encourage conservation on the part of energy consumers and to give additional incentives for exploration and production.

In response to a quadrupling of world prices in 1973-74, and the threefold increase in 1979-80, many consumers turned thermostats down in the winter and up in the summer. The effect of these temporary conservation measures and the impact on world economic growth showed up in declines in worldwide consumption of 3 million barrels per day in 1975, 3 million barrels per day in 1980, and an additional 3.6 million barrels per day in 1981.

More important than the short-term conservation measures were the long-term effects on consumption. New homes and commercial buildings increased heating efficiency through the use of increased insulation, heat pumps, and computer control systems. Industry developed more energy-efficient processes and implemented those processes in retrofitting existing equipment and in the installation of new equipment. Congress mandated that automobiles sold within the United States meet minimum mileage requirements.

The difference between the short-term measures and the use of insulation and improved technology is that the latter is more or less permanent. Even though the current low price of petroleum and its products might not justify the expense of increased efficiency in a new factory or building, those facilities built when it was cost-effective will continue to use less energy for 10-30 years.

Petroleum consumption worldwide, with the exception of 1975, increased from 1973 through 1979, when both short- and long-term effects of the two major price increases began to exhibit themselves in declines in consumption.

Since 1979, crude oil consumption has declined by almost 15 percent from 62.5 million barrels per day in 1979 to 53.4 in 1985.

In 1979, OPEC production totaled about 31 million barrels a day which was more than 49 percent of total production. Since that year, world consumption declined 9 million barrels a day but due to the increased incentives to explore for oil brought about by the two major price increases of the 1970's, non-OPEC countries in-

creased their production by almost 5 million barrels a day. OPEC, as a result, lost almost half of its 1979 production to a combination of conservation and increased production by non-OPEC countries.

As a final result, OPEC nations are faced with not only prices half of those experienced in 1980 but also with a similar decline in sales volume. That means a decline in gross OPEC sales of more than 70 percent.

Since crude oil is a major source of revenue for the majority of the members of OPEC, it is not unreasonable to expect that each of those countries will attempt to cheat on OPEC-imposed quotas in an attempt to increase revenues. The continued incentives to cheat on quotas caused Saudi Arabia to cut its production from almost 10 million barrels a day in 1980 to below 2.5 million barrels a day in August 1985 in an attempt to maintain prices. The reduction in production is roughly half that of OPEC as a whole. It was not unexpected that at some point Saudi Arabia, with a large current deficit, would demand a more equitable distribution of production costs among its OPEC partners and the current price of below \$10 a barrel illustrates that point.

If an agreement acceptable to Saudi Arabia cannot be reached at the April 15 meeting of the OPEC countries, the result will be a continuation of low crude prices. This will cause increases in consumption and decreases in production by non-OPEC producers. The result for the United States will be increases in consumption, a decline in domestic production, and an increase in imports. The increased level of imports will lead to another round of OPEC price increases in 3 to 5 years and, of course, it is inevitable that a continuation of current price levels will once again put the United States in the position where the interruption of imports would lead to repetition of the problems experienced during the Arab oil embargo and the Iranian revolution.

Faced with another energy crisis, the United States will attempt to increase exploration activity and production levels. The difficulties will mimic those of the 1970's. There will be a shortage of drilling rigs and equipment but even more important, there will be a shortage of human capital. The geologists and petroleum engineers currently being lost to other professions will have to be replaced. The replacement can take 5 to 10 years with the new replacements coming out of colleges, and universities, and needing several years to become experienced enough to become fully productive.

Other members of the panel have experienced, I am sure, in their oil and gas exploration production activities the difficulties of dealing with entering petroleum engineers and geologists. It is not an overnight situation. It is not like closing down a factory in Detroit, leaving all of the auto-producing facilities there so that at some point in time you can sort of within a 1- or 2-month period start the factory again. It takes 3, to 5, to 10 years to start the factory out here and we are not even talking about the time between when a seismic crew goes out and says this looks like a likely area, land deals are negotiated, contracts are negotiated, drilling rigs are obtained, contractors to do that, feeder lines are built if the well is successful, and remember this is a high-risk business. A very low percentage of new wildcat wells actually result in production. It is a high risk to capital and even high risk right now is the impact of

declining oil prices on our stock of human capital in this area which is necessary to production and a continued energy independence for the United States.

Many of the problems the country faced over the last few years could have been significantly reduced had the petroleum and natural gas industry not been regulated. If domestic crude prices had been allowed to increase with international prices in 1973, the United States would have faced higher energy prices earlier, encouraging more production and lower consumption. Conservation measures would have been adopted earlier and the impact of the Iranian revolution on international prices would have been reduced.

The regulation of the natural gas industry under the Natural Gas Act of 1938 and its successor the Natural Gas Policy Act of 1978 created similar problems. Multiple categories of price regulation under the NGPA shifted the emphasis away from exploration and production of low-cost shallow gas toward high-cost and high-price deep gas. In the absence of such price regulation, production would have been higher and average gas prices lower. The effect of the act was to shift production from low-cost supplies to high-cost supplies. The Fuel Use Act also limited the market for natural gas which could have been an effective substitute for petroleum in many applications. In the absence of the act the effect of substitution for petroleum would have meant a reduction in U.S. dependency on imports.

The windfall profit tax also had a negative impact on domestic production by effectively regulating prices and shifting emphasis away from the development of low-cost reserves and toward high-cost reserves and production.

In summary, the impact of much of the regulation of the energy industry ran counter to its intended purpose: increased energy independence and lower prices for consumers.

And with that I will conclude my remarks and refer you to the other testimony.

[Attachments to testimony follow:]

Table I

Refiner Acquisition Cost of Crude Oil¹
Dollars per Barrel

	Domestic	Imported	Composite
1974	7.18	12.52	9.07
1975	8.38	13.93	10.38
1976	8.84	13.48	10.89
1977	9.55	14.53	11.96
1978	10.61	14.57	12.46
1979	14.27	21.67	17.72
1980	24.23	33.89	28.07
1981	34.33	37.05	35.24
1982	31.22	33.55	31.87
1983	28.87	29.30	28.99
1984	28.53	28.88	28.63
1985	26.64	27.04	26.75

¹Source: U. S. Department of Energy

Table II

Midland and Odessa Employment

	<u>Price of Crude Oil</u>	<u>Wage & Salary Employment²</u>	<u>Manufacturing Employment²</u>	<u>Mining Employment²</u>
	<u>\$/Bbl</u>			
1975	8.38	68,260	7,730	13,510
1976	8.84	71,850	7,610	13,740
1977	9.55	78,360	8,970	15,040
1978	10.61	85,230	10,390	16,590
1979	14.27	87,800	10,470	16,960
1980	24.23	96,350	11,600	19,100
1981	34.33	110,800	14,300	22,100
1982	31.22	116,100	12,900	22,900
1983	28.87	102,500	9,600	20,500
1984	28.53	101,500	8,800	21,100
1985	26.64	101,600	8,900	20,600
1986 February		100,200	8,800	19,600

¹Refiner Acquisition Cost of Domestic Crude Oil, Source: Department of Energy

²Source: Texas Employment Commission

Table III
Odessa Employment

	<u>Price of Crude Oil</u>	<u>Wage & Salary Employment²</u>	<u>Manufacturing Employment²</u>	<u>Mining Employment²</u>
	<u>\$/Bbl</u>			
1975	8.38	39,940	5,500	6,320
1976	8.84	42,360	5,720	6,380
1977	9.55	45,340	5,960	6,960
1978	10.61	48,360	6,530	7,490
1979	14.27	49,250	6,850	7,560
1980	24.23	53,050	7,450	8,150
1981	34.33	60,550	9,450	9,350
1982	31.22	62,100	8,400	9,300
1983	28.87	52,800	5,800	8,400
1984	28.53	51,300	5,100	8,700
1985	26.64	52,200	5,200	9,000
1986 February		51,300	5,000	8,700

¹Refiner Acquisition Cost of Domestic Crude Oil, Source: Department of Energy

²Source: Texas Employment Commission

Table IV
Midland Employment

	Price of Crude Oil	Wage & Salary Employment ²	Manufacturing Employment ²	Mining Employment ²
	<u>\$/Bbl</u>			
1975	8.38	28,320	2,230	7,190
1976	8.84	29,490	1,890	7,360
1977	9.55	33,020	3,010	8,080
1978	10.61	36,870	3,860	9,100
1979	14.27	38,550	3,620	9,400
1980	24.23	43,300	4,150	10,950
1981	34.33	50,250	4,850	12,750
1982	31.22	54,000	4,500	13,600
1983	28.87	49,700	3,800	12,100
1984	28.53	50,200	3,700	12,400
1985	26.64	49,400	3,700	11,600
1986 February		48,900	3,800	10,900

¹Refiner Acquisition Cost of Domestic Crude Oil, Source: Department of Energy

²Source: Texas Employment Commission

Table V

U. S. Seismic Crews and Rotary Rigs¹

	Crews Engaged in Seismic Exploration <u>Average</u>	Rotary Rigs in Operation <u>Average</u>
	<u>Monthly</u>	<u>Weekly</u>
1973	250	1,194
1974	305	1,472
1975	284	1,660
1976	262	1,658
1977	308	2,001
1978	352	2,259
1979	400	2,177
1980	530	2,909
1981	681	3,970
1982	588	3,105
1983	473	2,232
1984	494	2,428
1985	378	1,980
1986 Current	292	1,063

¹Source: Department of Energy

Mr. STENHOLM. Thank you, Mr. Williams. Next we will hear from Mr. Buzz Hurt, independent oil producer, Odessa, TX.

**TESTIMONY OF JAMES RATLIFF HURT, INDEPENDENT OIL
OPERATOR, ODESSA, TX**

Mr. HURT. Thank you for the opportunity to testify here today. My name is James Ratliff Hurt. And as you called me, I am better known as "Buzz" around here but I have been an independent oil operator in the Permian basin since 1963.

The oil industry has a history of boom and bust. But this cycle we are seeing has the most extreme excesses in both directions. During the OPEC embargo of the 1970's with its shortages and gas lines, there was a consensus of energy experts who believed that this country was running out of oil and natural gas, that this country was in the moral equivalent to war, that this country should have a national energy policy. By the way, whatever happened to that national energy policy?

What happened out here after the embargo was that domestic oil prices soared thanks to OPEC. Those of us in the business certainly had much more income. However, the rest of the Nation was saddled with paying for inflated prices for fuel. We in the oil industry seemed to be at cross purposes with the rest of the Nation. All of a sudden after years of hard work and gambling my hard-earned

money to find more oil, I was being called a bad guy all because some foreign ministers in nations far away from Odessa, TX, decided to stop producing as much oil.

Because of that OPEC decision, which no one consulted me about, I became strapped with the Federal Energy Regulation Commission for gas production—out here we call it FERC—and with the windfall profits tax for oil production. FERC, which amounted to continued price controls on natural gas, was so complicated I had to hire a team of legal experts to tell me how to comply with the law. The windfall profit tax has been nothing but a terrible administrative and financial burden. Ask my accountant or any other oilman's accountant.

But never mind the Government restrictions, the experts were projecting that the price of oil would soon rise to \$70 a barrel. So we borrowed money on that basis so we could drill for more oil. We believed these projections, so did the banks, so did everyone. However, in 1981, the price went down. Banks, independents, engineers, geologists went down. The FDIC is now the biggest operator in the oil patch.

This year the price of oil has had an even worse drop which means an even deeper impact on what I am trying to do. Because of the turmoil within OPEC, I have no idea what is going to happen to the prices. This makes it difficult to continue the economics of projects I have planned this year. The uncertainty of tax law also compounds its difficulty. Every time I read about Congress simplifying the tax laws, I see how complicated the proposals are and how, almost without exception, the incentives for oil exploration are taken away.

But while OPEC and the proposed tax laws continue to cause my income figures to fluctuate, some of my other figures remain the same. No bank has ever seen fit to lower the amount of my principal because the price of oil has declined.

So here is a question I would ask: Is it really in the national interest to have a weak domestic oil industry and cheap energy prices when this condition could swing in the opposite direction at the whims of some foreign ministers in Saudi Arabia? Those experts I talked about earlier were right about one thing, we do need a national energy policy.

In this policy, I would urge Congress to at least maintain the current tax incentives for the oil industry. With its shrinking tax base, the small cost of these incentives to the Treasury is well worth the chance it gives to the survivors in this industry. The fewer survivors, the weaker the industry will be. You just cannot turn the tap back on.

While we are at it, let us scrap the windfall profit tax, first, because currently the cost to the Treasury would be zero. This would be another incentive to the survivors in this business. We could look forward to the price stabilizing and increasing enough to see better economics.

Mr. STENHOLM. Thank you, Mr. Hurt. Next, Mr. Sam Holloman, Sam Holloman Cos., Odessa, TX.

TESTIMONY OF SAM HOLLOMAN, SAM HOLLOMAN COS.,
ODESSA, TX

Mr. HOLLOMAN. Mr. Chairman, Congressman, I am a contractor, oilfield contractor. I make a living doing about everything that is needed to produce oil once it is drilled and found. I own a service company called Holloman Construction Co. It is my main income, my main line of business. I am very concerned about the future of it and all of west Texas.

Our oil industry was changed from a boom to a bust situation back in 1982 and we refer to that locally as happening one day while we were at lunch because it was almost that sudden. The washout got all the doctors out of the oil business and all of the teachers out of the machine shop business and got us all back to doing what we do best. It was a healthy weeding out. The ensuing years since 1982 has seen the survivors of this period become extremely efficient businessmen. We have drilled more holes. We have laid more pipeline. We have done more of everything with less people and equipment than we ever thought possible.

Only recently have these companies come to show a little profit from 1982. At this time, the survivors from the first downturn need anything but for the price of oil to go down. The present slide in prices has delayed or halted many of the projects that we make a living on. It is almost completely halting the wildcat drilling programs.

At the same time, we are being hit with a tax reform law that looks like it will make a bad situation even worse. I personally support tax reform but I feel it will further dry up the funds available for drilling ventures. My personal wildcatting experience has been two very dry holes and without a very good tax incentive, I assure you, no more of my money will go to that end. I believe if oil prices rise, which they must do, then the industry could survive tax reform.

In my line of business, the investment tax credit plays a big part. It decides when and how much equipment we purchase. In years of good profit, it is always easier to gamble on the future if there is a tax advantage to it. Here again, if our industry will stabilize where there is not such a boom-and-bust, high-risk business, we might very well survive without ITC. Stabilization is the thing most lacking in the oil industry at this time.

At the present prices of oil and with the pressure on gas to compete, the following things will happen to our industry. Almost all wildcat drilling will cease. The remaining healthy companies that are needed to produce oil will dwindle to a very few, if any. There are too many of us that are just recovering from the downturn. Many banks and savings and loans in the energy section already heavily burdened with loan losses will close their doors. I personally have sold my bank stock, resigned my bank board, and gotten out. Domestic oil production will drop severely and oil imports will rise. OPEC, or maybe in the future it may be Britain, or Norway, or Mexico, or whoever produces lots of oil will have the same opportunity to severely raise prices and I say it is going to do the same thing over again.

As to the matter of defense, there should be a magic number that we need in our industry for it to be healthy. At the local level, \$25 seems to be the minimum that we need to survive and keep a healthy domestic industry. How do we get it there? I personally favor a diminishing import tax, a lot of people do not. The problem here is that every time tax is mentioned in the oil business, the worst taxes get zapped on our domestic industry making it again less able to compete.

If in my previous analogies domestic oil production dwindles, what about our defense? Our strategic reserve would serve us for a time if it could meet the production and distribution needs. Fortunately, we have a feasible network of oil and gas lines across this country that have been laid by a healthy petroleum industry. Nothing will let us sleep well at night like having our own supplies of fuel. All of America's cheap oil is drilled out, but worlds of reserves lie undiscovered in offshore lands and deep formations. General Rommel's Desert Corps attest to what happens without your own fuel.

This is a big what if, but what if the next war would be fought on American soil. How many tanker loads of oil could we depend on to sneak past modern radar and missiles. We could never gear up a dead industry to do the things needed to produce from our own reserves, reserves still undiscovered because of short-term flood of cheap oil. We have been held at ransom for not having our own oil and found out how quickly things can ground to a stop. Must we have a war at the same time to alert this country to the stupidity of not having our own energy?

Even now a neighbor to the south and an oil-rich OPEC country border on a war with us. Our people must always be ready. We have another neighbor, Mexico, that is a potential problem. Everyone says we must treat Mexico differently, that if there is an import tax, we cannot tax their oil. I don't know why this is. I don't think it should befall us to be Mexico's keeper. My philosophy about Mexico is if she cannot support herself—this is a little radical—maybe she should become the 51st State of the United States. Maybe Nicaragua should be the 52d.

I don't believe the United States is rich enough any more to heal the world's problems. I think it is time to look after ourselves and do what we need to do. If 10 million Mexicans want to be U.S. citizens, maybe the whole country should be, a radical point of view. But what would the outcome be if we did the development of their oil reserve and development of resources that Mexico could never do; raise the living standards of every poor Mexican. Maybe it's time for drastic action. Please pardon this radical ending.

[Mr. Holloman's prepared statement follows:]

PREPARED STATEMENT OF SAM HOLLOMAN, SAM
HOLLOMAN COS., ODESSA, TX

March 24, 1986

REPORT TO CONGRESSIONAL SUB COMMITTEE

Gentlemen:

Concerning the impact of the current oil prices on the future of the oil industry and as to its effect on national defense, I would like to submit the following information, as I see it. I am the owner of a Service Company who supplies men and equipment to be utilized in the production of oil and gas.

1. LOCAL EFFECTS:

The oil industry was changed from "boom" to a "bust" situation in 1982. We refer to it locally as happening "one day while we were at lunch". The wash out that followed got all the doctors out of the oil business, all the teachers out of the machine shop business and resulted in a general healthy weeding out of the inefficient. The surviving companies can compete very efficiently and most of us suffered through a year or two of losses, but have recently returned to profitability. The drilling rig count, of course, had declined tremendously but was offset a lot by increased efficiency, as were most service company operations (including mine). We are all able to do more work with fewer men and equipment. The price of oil had risen to nearly \$40, and even at \$30, there was enough profit in it to sustain the giant CO₂ flooding projects which will produce so much oil for this country.

The present slide in prices has halted or delayed many of these projects. It is also almost completely halting the wildcat drilling programs necessary for our Petroleum reserves to be replenished.

At the same time a tax reform law is pending to make a bad situation even worse. While I support the reform, I feel it will even further dry up the funds available for these drilling ventures. Wildcatting is for the very brave and I have two dry holes as my venture into this unknown. Without some form of tax incentive, I can assure you no more of my funds will go to such ventures.

I do believe if oil prices rise, (which they must eventually do) then the industry could survive tax reform.

In my line of business, I.T.C. plays a big part in deciding when and how much equipment to purchase. In good profit years it is always easier to gamble on the future if there is a tax advantage to it. Here again, if our industry will stabilize where it is not such a boom and bust, high risk, business, then we might very well survive with out any I.T.C. Stabilization is the thing most lacking at this time.

At the present prices of oil, and with the pressure on gas to compete, our industry will do the following:

- (1) Almost all wildcat drilling will cease
- (2) The remaining healthy companies that are needed to produce oil will dwindle to a very few. There are too many of us just recovering from the last downturn.
- (3) All Banks and Savings and Loans, in the energy section, already heavily burdened with huge losses, will close their doors.
- (4) Domestic Oil production will drop severely and oil imports will rise.
- (5) O.P.E.C. (or Brittain and Norway or Mexico or others) will seize the opportunity to severely raise prices and we will go thru the same thing all over. Maybe much worse.

II. DEFENSE:

What is the magic number (\$) that oil must bring for a healthy industry? \$25 seems to be the majority view. How do we keep it there? Maybe with a diminishing import tax. The problem here seems that everytime tax is mentioned in the oil business, the worst taxes get zapped on our domestic industry, making it less able to compete. If, in my previous analogy, domestic production dwindles, what about defense. Our strategic reserve would serve us for a time, if it could meet the production and distribution needs. We have a beautiful network of oil and gas lines across this country laid by a healthy petroleum industry.

Nothing will let us sleep well at night like having our own supplies of fuel. All of America's cheap oil is drilled out, but worlds of reserves lie undiscovered in offshore lands and deep formations. General Rommel's Desert Corp can well attest to what can happen without your own fuel reserves. What if the next war would be fought on our own soil (heaven forbid). How many tanker loads of oil could we sneak past modern radar and missiles. We could never gear up a dead industry to do the things needed to produce from our own reserves. Reserves still undiscovered because of the short term flood of cheap oil. We have been held at ransom for not having our own oil and found out how quickly things ground to a stop. Must we have a war at the same time to alert this country to the stupidity of not having our own energy. Even now a neighbor to the South and an oil rich O.P.E.C. country border on a war with us. We must be ready.

We have another neighbor (Mexico) that every one says must be treated differently. If we tax oil, we cannot tax theirs. I don't know why. Why has it befallen us to be Mexico's keeper? My philosophy about Mexico is that if she cannot support herself, maybe she should become the 51st state of the United States. Maybe Nicaragua should be the 52nd. I don't believe the U.S. is rich enough anymore to heal the world's problems. I think it is time to look after ourselves and do what we need to. If ten million Mexicans want to be U.S. citizens, maybe the whole country should be. A radical point of view? Maybe. But what would the outcome be if we did. Development of an oil reserve, and development of resources that Mexico could never do herself. Plus raising the living standard of every poor Mexican. Maybe its time for drastic action.

Mr. STENHOLM. Thank you, Mr. Holloman. Next we will hear from Mr. Ron Fancher, president, Texas Commerce Bank, Odessa.

TESTIMONY OF RONALD L. FANCHER, PRESIDENT AND CHIEF EXECUTIVE OFFICER, TEXAS COMMERCE BANK, ODESSA, TX

Mr. FANCHER. Good morning, gentlemen. I'm Ron Fancher of Odessa, TX. I speak to you this morning as an individual who was born, raised and educated in west Texas. I spent my early years on the family farm near Olton, 200 miles north of here and studied business at West Texas State University in Canyon. My business career involves 20 years as a commercial banker in Lubbock and in Abilene, finally in Odessa where I serve as president and chief executive officer of Texas Commerce Bank, a concern which only recently celebrated its 30th anniversary in this community.

The heritage of west Texas is one of fierce, if not stubborn independence. We take great pride in our individuality and our ability to get the job done without a great deal of assistance and without much regard to personal sacrifice. Through the years we've asked little of those outside the area and forged a strong regional economic base centered around the natural resources of the area, first agriculture but in recent years and in particular in the Permian Basin predominantly around the oil and gas business. Today it's safe to say that we're virtually dependent upon oil and gas as a basis of our economic atmosphere. Our substantial manufacturing complex has and continues to cater to drilling production and transmission demands of the industry. We provide a regional base for most major oil companies, most major gas producers and for an untold number of independent producers of all sizes.

As you are well aware, the Permian Basin accounts for roughly 30 percent of the existing known oil and gas reserves in this Nation. During the past 30 years we have seen a new chemical industry spring up from efforts of area leaders to make use of natural gas which we previously flared at the well head. Today the industrial complex south of Odessa represents the largest inland petrochemical complex in the Nation. It adds materially to our product and employment base.

In light of our dependence on these great natural resources, we recognize the need to diversify our economy. While this effort continues, its result will be felt over an extended period of time rather

than offering immediate dilution to our energy dependence. We have long ago recognized education as a predominant right and need. Our local communities have over the years produced a system of primary and secondary schools second to none. Local and State taxes from a strong real estate and energy base over the years have also supported a growing junior and senior college and university system in the area. These institutions today are closely tied to our diversification efforts and provide a focal point toward these efforts as we attempt to build and expand upon the tremendous base already in existence.

Today we are faced with a great dilemma brought about by the nature of any commodity business, whether contrived or not, an imbalance in supply and demand. Our area boomed in the late 1970's and early 1980's as our Nation rushed to become energy independent in the face of rapidly increasing product costs. During that period of time, development money poured into the area. Economic growth was, to say the very least, substantial.

In 1981, prices peaked and backed off. Our Nation became comfortable or complacent with a 30-percent dependence on imported oil, a situation that sees us absorbing our energy reserves at a rate equal to 120 percent of those being replaced annually. Growth in our area cooled. For the past 4 years, we've weathered the collapse in natural gas prices and a general constant decline in the oil industry. During that period, we have observed reductions in population and work force and increases in unemployment. Vacancy rates in residential and commercial properties have skyrocketed. Property values have plummeted.

Personal and business bankruptcies have soared as business failures have become commonplace. For the first time since the 1930's, we have observed bank failures first hand on a multiple scale.

Most recently we've seen a total collapse in crude oil prices. An immediate result has been the curtailment of capital expenditure budgets from major and independent operators alike. Drilling activity represents at least a 45-percent decline from a year ago. The number of rigs working nationwide has declined better than a third since last October and more than 50 percent since 1982. February's sales tax receipts in Midland and Odessa are running approximately a third below comparable periods in 1985. Unemployment levels in both communities have increased 50 percent or more since the year began, standing in excess of 7 percent in Midland and 9 percent in Odessa at the end of February already near the worse figures that we saw in 1982 and 1983. Long term planning is to say the least at a stand still and short term decision making in the area today is tentative at best.

In the face of these problems, we are still confronted with the threat of new tax burdens through changes and the treatment of the intangible drilling costs and the depletion allowance. We find this possibility even more frustrating in light of the fact that our basic industry already bears an inordinate tax burden in the excise tax commonly called the windfall profits tax and the fact that the Fuel Use Act places many traditional gas users off limit to our natural gas industry.

Ours is a capital intensive industry unlike any other in the economy. Heavy costs and risks of developing new oil and gas reserves

are well known. All income is treated at ordinary tax rates but unlike other capital intensive investments, no residual remains after the asset is depreciated. The depletion allowance, more particularly, the percentage depletion allowance provides the only similarity to capital gains tax treatment available to other industries. This allowance has been subjected to 6 separate increases or restrictions in the past 15 years.

The timing and availability of beneficial tax treatments for intangible drilling costs has been addressed no less than five times in that period. Current treatment to some extent addresses the inherent nature of well life in that production is heavier toward the front end. Logically, the heavy part of the depreciable portion of the asset should be weighted as near the front end as possible. To do less would severely inhibit the industry's ability to attract and retain funds.

Gentlemen, the windfall profits tax is a dinosaur. It addresses a situation which certainly no longer and perhaps never did exist. It should be repealed.

The Fuel Use Act has produced radically reduced markets for natural gas reserves and has resulted in the inability of the industry to adequately plan for the distribution of a product available in abundance. On the other side it's resulted in uneconomic conversions of power plants to alternative fuels in some cases.

The shipment of coal thousands of miles to a powerplant located in the heart of the oil patch near existing wells waiting for a market seems to make little sense. Priorities appear to be flawed when we fail to consider local and industry economics as well as environmental and national objectives. It is important that we consider the fact that the oil and gas business locally and nationally is one of great economic benefit and the fact equally stated that it is a sick business today. The industry faces tremendous problems in attracting funds for replacement of our steadily declining reserves.

Our national security is severely threatened as long as we remain inattentive to our growing dependence on foreign oil or our energy reserves in the future. We must not allow ourselves to look at the industry continually as an easy touch from a taxation standpoint or the industry will not survive as we know it, much less prosper.

Our goals of local and national economic prosperity and energy independence are closely related today. I see the choices as rather clear. We must loosen the reins of taxation and regulation. To do less will strangle the industry and in that scenario the Permian Basin's economic well being will be severely depressed for many years to come. Even worse, I believe the Nation as a whole will be poised for a stormy future largely influenced by forces beyond its own control.

Mr. STENHOLM. Thank you, Mr. Fancher. Next we will hear from Mr. Charles Perry, Perry Management, Odessa, TX.

**TESTIMONY OF CHARLES R. PERRY, PERRY MANAGEMENT,
ODESSA, TX**

Mr. PERRY. Mr. Chairman, thank you very much for the opportunity of appearing here today before this subcommittee. My name is

Charles R. Perry, and I live in Odessa, TX. I also serve as chairman of the board of MBank-Odessa, approximately a \$225 million local bank, but I would like to qualify my banking relationship by saying that I am not a career banker although I am active on the loan committee and executive committee. My background is the oil and gas industry and I am an engineer. I merely serve as an outside director but I will attempt today to relate to you how the economic conditions in this area are impacting the local banks and their customers. Perhaps I should speak more as a customer, I borrow a whole lot more money than anything else so I am wearing two hats in that respect.

The recent decline in oil and gas prices have left many of our customers in shock. Most were apprehensive about the future of the oil and gas industry with the passage of the Rostenkowski tax bill last December by the House of Representatives which would clearly reduce tax benefits that were originally designed to encourage drilling exploration. However, the recent price decline made these tax problems appear to be minimal compared to the most urgent immediate problem of reduction by 50 percent in gross revenues. In this particular area, our stronger banks are entering this drastic turn down with relatively good equity positions but in some cases perhaps insufficient loan loss reserves. However, most of the stronger banks have relatively low loan-to-deposit ratios which indicates a very good liquidity and I'm talking about in a 50-55-percent range.

Our weaker banks also enter this period with good equity. Some of them have had capital infusions, some of them have managed to get themselves in better shape, and they also have good loan loss reserves. However, probably these loan loss reserves are going to be needed. They do have higher loan to deposit ratios, up in the 65- to 70-percent range, which certainly will make these banks more susceptible to loss of depositor confidence with the lower liquidity.

Although most people would consider the banks in this area as energy banks, I think energy loans do not represent perhaps the greatest potential problem. Although we do have our share of poor quality energy loans, a large number have been identified over the past 3 years and have either been written off or foreclosed on or collected. However, we now find problem loans appearing in other parts of the loan portfolios, mostly real estate. Because of the poor economy here and the related lack of liquidity of all of the customers, we find that loans are continually plagued with a lack of secondary source of repayment. To aggravate the problem further, collateral may be of little value since it is not saleable even if foreclosed upon; because of the lack of liquidity of most of the principals involved in these various related ventures, their guaranties have very limited value since it would be difficult to collect under them when the guarantor has no liquidity also.

Perhaps even more disturbing is the deterioration of the attitude of our borrowers. They have become quite defensive, and they tend to withdraw and attempt to take care of themselves. Perhaps in this type of economic climate, this merely means survival is of utmost importance. There appears to be little reservation on the part of borrowers to utilize the bankruptcy laws to face these problems. Bankruptcies of course are running at an all time high.

Although we have seen very little deterioration at this time in consumer loans, we can expect that delinquencies will pick up considerably in the next 2 to 3 months as the impact of lay offs, reduced salaries, and unemployment begin to take their toll. There are several outcomes that we can reasonably expect to occur within the banking industry as a result of the reduction in oil prices and the impact of more punitive taxes proposed. These include: First, I think we can expect very shortly to have classified loans equal to 100 percent or greater of equity in a large number of banks in the area. Although this may be an overreaction compared to what actual loan losses will ultimately occur, it does represent a conservative attitude on the part of the banks to address problem loans as early as possible.

It is too early to tell what the impact in terms of actual loan losses are but I believe that these will be reduced somewhat by the tendencies of banks to rapidly face these problem loans.

Second, we can expect earnings to dwindle with the stronger banks approaching zero earnings and therefore no appreciable increase in their capital. In the weaker banks we can expect capital accounts to actually decline as losses occur.

Third, the banks within this area can expect to shrink in size as reduced income results in reduction of deposits and quality loan demand, as the demand for them will dwindle. This of course will result in lay off in bank personnel as the banks shrink in size. Let me put it in summary: As the economy dwindles, we just don't need as big of a bank as we have today.

Fourth, banks will lose quality loan customers due to the tendency that we are seeing right now, stronger customers to liquidate and cease operation in this atmosphere. This tendency towards liquidation on the part of our stronger customers is being caused both by down turn in the demand of their products and services and by an increase in cost of liability, workmen's compensation, and general casualty insurance which came incidentally at the same time.

We have premiums that are frequently running as high as 500 percent to 1000 percent higher than comparable premiums a year ago. In some cases I have seen the insurance policy premium actually run as high as 30 percent of revenues in a particular operation. Although banks in this area may well tighten their belts and reduce themselves in size, reduce employment and may not even be profitable, nevertheless, in my opinion most of them will survive. The banks actually should weather this turn down in a lot better shape than the general economy of the area and probably their customers.

This is due primarily to the fact that banks have operated much more conservatively in the last 3 years than they did in the early 1980's and as a result have a much stronger loan portfolio now than they did in the 1981-82 era.

We have one major plea for your assistance in the banking industry in this area and our plea is simply this, that from a regulatory standpoint, we be treated no differently than the major money center banks are treated in evaluation of their loan portfolio with respect to their energy related foreign loans.

We strongly believe that if we could treat our customers with the same degree of leniency that the large money center banks are

able to treat their foreign customers it would allow us to work with many of our better customers in a manner which would allow them to survive until there is some recovery in the oil and gas industry. If this is not done, when a need arises in years to come that we rejuvenate the domestic energy business, there may well be no service and supply companies or competent technical personnel left.

Thank you very much for the opportunity of appearing before you today. Should you require any further information, please feel free to call on me.

Mr. STENHOLM. Thank you, Mr. Perry and thank all of you for your very excellent, very thought provoking, and very factual testimony this morning. I will recognize my colleague Mr. Combest for any questions he might ask of you.

Mr. COMBEST. Mr. Chairman, thank you. I would also like to compliment you on your testimony. I had a whole list of questions about specifics, and you have answered a lot of those. Your testimony has been very factual and certainly direct. I guess that is what we are looking for, some answers to know exactly which direction to go. As all of you have pointed out, a number of the different areas have to be addressed relative to energy policy. An energy policy is going to have to deal with taxes, it is going to have to deal with regulations; regulation in the industry as well as regulation in the banks, and many other areas including something that hopefully will provide some optimism rather than continued pessimism in the industry.

In the area of banking, the industry regulation, and all of you feel free please to respond, I guess I am just directing my question to Mr. Perry and Mr. Fancher because of their direct involvement. Maybe I should direct it to you, Mr. Holloman, since you are out of the banking business at the present time. What specifically, or what are some of the specific things, that we might be able to do in banking regulation that would help ease present conditions? Obviously, we do not want to make it a situation where those restrictions are taken away to the extent that the banking industry becomes insolvent or does not have to deal with its own problems, but what specifically are some of the things that we might be able to do or that we can legislate, specifically, rather than in general terms, where that is left up to the interpretation and the goodwill of the man that comes into your bank and examines it?

Mr. FANCHER. I think the first thing that we need to do, Mr. Congressman, is to look at the situation that a bank to be a viable enterprise over time must be profitable and it must plan as far ahead in the future as it can for contingencies that may exist from time to time. One thing that is pending today is a proposed change that would not give a bank the continuing ability to reserve for future loan losses out of current income but rather to take current losses out of current income.

In my estimation, that is a very poor way to plan. I think it is absolutely impossible to see that kind of a loan loss reserve charged to income being effective in this market today. I do not believe that that is limited to the Permian Basin. I think you can take that into the agricultural sector and find that I think in the agricultural area whether it be in West Texas or in Iowa is faced

with the same problems that a bank in the Permian Basin is faced with from the standpoint of anticipating declines in its home market over time.

There are a number of suggestions pending regarding changes and equity capital requirements of things. My bank is fortunate in that it has a very strong equity position today. The company that owns my bank also benefits from a very strong equity position today. We need to be cautious in maintaining reasonable equity requirements in things. But we do not need to get carried away with thinking that we can arbitrarily legislate equity in financial institutions today. The returns that financial institutions are producing today are not what they were years ago and it may be more difficult in the future and it is certainly difficult today to attract new equity capital into these businesses outright.

Another thing that I see being rumored and talked about repeatedly is changes in the treatment of tax free income on municipal securities. I think that would be devastating not only to the financial institutions in the country, to pension plans, to profit-sharing plans, to many other institutional types of investors who do not necessarily invest for themselves but invest the moneys of millions of individuals deposited with them for safe keeping and for future use. I do not believe this is the time to tamper with the basic fabric of the tax structure relative to our financial institutions. They are troubled, there is no question but what in the southwest they are troubled and it is not a situation that is going to turn around right away.

Mr. COMBEST. You spent a long period of time talking about the tax bill and all of our love-hate relationship with that. You mentioned, Mr. Fancher, that there were proposals for making some of the changes in loan loss ratios. Where is that proposal?

Mr. FANCHER. This is a proposal that has been on the IRS's agenda for a long time, Larry. I believe it was deferred as I recall 1 or 2 years ago. We were supposed to have gone to a situation where we did not maintain a reserve, but expense current losses and current years. That has been deferred. I know the conversation on it is a continuing affair.

Mr. PERRY. Along that same line at this time in the regulatory atmosphere, loan loss reserves are construed to be part of capital, and I do not know how Mr. Fancher feels, but I do not agree with that. If you set up a loan loss reserve, it is because you expect to lose it and the old rule of thumb, of banks having a range of 6.5 percent of assets, to capital, I think is still a good one. But I would not include loan loss reserves as part of that capital. What I alluded to in terms of the manner in which the foreign loans are treated—

Mr. COMBEST. That will be my question.

Mr. PERRY [continuing]. Is and a plea for a change in the regulatory atmosphere is probably construed to be a nonperforming loan. If we have a nonperforming loan here, it is one in which the principal reductions are not being made. The interest can be paid current and it can be nonperforming. It can be nonperforming if the primary source of repayment no longer exists, and you have to look at the secondary sources.

This is occurring all the time in foreign loans and they're not being classified. But under the same circumstances, we find ourselves having to classify them. In one case I even know of, one loan that had a secondary collateral pledge, which was New York Stock Exchange listed stock, and the loan was classified because the primary source of repayment, which was sale of real estate, did not exist. In other words, there was no market for the sale of the real estate. And some of these things I think are an overreaction.

I think the other side of it, the good news is that the banks are now stronger because of that overreaction that has occurred in the last 3 years, and, therefore, that is the reason I feel we're in better shape to weather the storm than we would have been otherwise.

Mr. COMBEST. Quickly on that subject, Mr. Perry. Is there a specific regulation difference that allows dealing with those banks separately, or is it the interpretation?

Mr. PERRY. I cannot answer that. Mr. Fancher may do it but I have wondered that myself.

Mr. FANCHER. I believe it is interpretation. I do not see any, of course I do not see the guidelines that the regulatory authorities use in underwriting the portfolios of banks. But I do believe that the criteria are assessed differently in different markets.

Mr. COMBEST. Regulation as it specifically applies is one thing to deal with, but an individual's interpretation and the broad latitude that entails, is sometimes very difficult to deal with. We hear horror stories here, and while I am not jumping on any Federal regulatory agency, there are always two sides to a story, we do hear some things that concern me a great deal. Although there certainly has to be some flexibility, the flexibility allows one a great deal of latitude, and that becomes very difficult to regulate and very difficult to control. It is very difficult to change sometimes without changing the attitude and that sometimes is difficult, too.

These are things that I think certainly have to be addressed. Again, they tend not to weaken the system, but the intent being to be somewhat realistic, I suppose, on what it is that we are doing. I am sure I have used up my time for questioning. I thank you, Mr. Chairman.

Mr. STENHOLM. Following up on that last line of questioning concerning banking and regulatory processes, I just had an experience in my own district, with a smaller rural bank that had three loans classified wherein the interest payments were current, but no principal had been paid. In each of the three individual cases, when confronted with the problem, the individuals wrote out a check for the amount of their loan and paid it off, and walked out of the bank, and took their business elsewhere. Now that suggests to me that there is an overinterpretation of the regulations by someone, and it came as a shock to me because it occurred within the last 3 weeks, as supposedly we are beginning to see some change in the regulations, as they deal with the problems we have in the energy business, and in the agricultural business.

So we are going to be following developments very closely to see that what we are told in Washington is, in fact, occurring. Mr. Perry, I agree with you that much of that which we have had to do has turned out to save us. Had we not begun to tighten up 3 or 4

years ago, we would be in much worse shape than we are today, and things are bad enough today.

The question that I want to ask all of you centers around what was a common thread throughout all of your testimony. We heard about the need for a national energy policy. I think there is a general agreement that boom and bust is not healthy for anyone. In the oil patch, we were not complaining when we were booming, but we are complaining when we are busting. Consumers were doing plenty of complaining when we were booming and that sentiment resulted in the windfall profits tax and some of the other changes in the Tax Code which have been unfavorable to the energy industry. Somehow the challenge to Congress and the administration is to find the middle ground, to find a national policy that will provide stability. Is stability in pricing good, Mr. Williams?

Mr. WILLIAMS. Well, I think that the answer to that is definitely yes. Stability in pricing is good particularly from the production side of things. If you have looked at consumption figures, of course we have seen significant declines in consumption both nationally and world wide. But the swings take place on the production side of things and those are the swings in our local economy, those are swings in North Sea oil production in response to massive price changes. And there is a tremendous reallocation of resources from one area to another, from one sector to another, with major price swings in energy. And the difficulty is that it takes so long for production to react to price changes, particularly when we have a reduced size of our interest structure, not enough petroleum geologists, not enough engineers.

You know it takes us 3 to 4 to 5 years to react to an upswing in prices which there will be. And there is some strategic implications obviously. Right now we are importing 30 percent of our petroleum. We could easily be, as I think you mentioned in your opening remarks, at 50 percent imports within a matter of years. The United States, with all of the efforts that we have seen in the Permian Basin and the rest of the United States, went from a rate count up to as high as 4,000, now we are down at 1,000. We barely made any changes, any significant changes in total U.S. production during that period.

Any benefits that we gained were more on the consumption side and we had to do all of these efforts just to stay even. And we are high cost producers. In the absence of price stability you have increased risk, increased risk means that higher priced capital coming into the industry. You know a gentleman like Mr. Hurt, Mr. Holloman who are directly involved in the drilling industry, you know probably right now are taking what capital they may have left after their current instability and perhaps looking at other places to invest it. And the next time around they might not be so willing to be in the oil industry or at least to as great of an extent.

And that has significant strategic implications for the United States. The problem is, how do we—and I am not sure that I have the solution. I think this is the reason that we need a long term energy policy and I think it needs to be a very serious thing and I know long term things are very difficult for Congress. You know

you folks are not elected for 20 years. But this policy needs to have a 20-, 30-year time horizon because of the strategic implications.

We will, in response to the current price decline, experience a tremendous production decline in the United States. We are high cost producers relative to the people who control prices. We are one of the world's highest cost producers on many of our wells, particularly the stripper wells. We can lose a million barrels a day production and that was very hard gain production. It was very hard to maintain and it took a lot of effort to do so. We need a long term energy policy that in a sense is divorced from the vagaries of annual or semiannual politics, biannual I guess I meant to say.

I am not sure what the policy should be. The thing that comes to mind obviously is an import tax on crude oil. That is one method for maintaining domestic price stability. We cannot control international markets obviously. The problem with an import tax on crude oils is it is virtually impossible to enforce or implement. If you taxed crude oil coming in at the gate, you know coming into the country then that means that domestic refineries are going to face higher prices. Their products, by the time it gets into the petrochemical industry will not be competitive on an international market because they are paying a higher cost for their feed stock by the amount of the increase in an import tax.

So, if you have a tax on imports of crude oil, you are going to have an import tax on refined products. Should that tax be one for one and just let flow \$5 or \$10 a barrel through, I do not know. But if you flow it through to the refiners, the petrochemical industry is going to be at a cost disadvantage internationally. If you let that import tax and you put it on crude oil imports, on refined product imports, on petrochemical imports, that is going to put our plastics industry at a disadvantage in international markets. You know there is no place to end this, make it clear to the automobile manufacturer who would be at a disadvantage paying higher costs for the plastics and the metal going into their products, put them at a disadvantage against the Japanese without an import tax.

Price stability is a very difficult thing to achieve. I do not know what method is workable but on the other hand, for a viable industry, we need some; we need price stability. I do not see any short term solutions, Mr. Chairman, I wish I did. I wish I could recommend to the committee a way to impose an import tax, a variable import tax that would move up and down with the price of crude oil to add some stability to domestic pricing and therefore domestic exploration production. I do not know how to implement that.

On the other hand it is a virtual necessity if we do not want to be in a very weak strategic position and certainly we will be there within 3 to 5 years.

Mr. STENHOLM. You have done a very eloquent job of explaining the pro's and the con's of an oil import fee. You have also demonstrated why it is said that Congress cannot make long range solutions in those years divisible by two or those immediately preceding those years divisible by two. You explained it very well. Mr. Hurt and Mr. Holloman are both producers. Do you agree that stable prices would be better for the industry as well as the consumer?

Mr. HURT. Yes, certainly.

Mr. HOLLOMAN. Yes.

Mr. STENHOLM. We all agree that the consumer does not benefit from boom and bust cycles. The question is how do you provide stability, particularly in a business which we do not control? The United States no longer controls the energy business. This control rests in the Middle East, which is very politically volatile. Do you have any suggestions other than the ones you have already given? Tax relief to our producers does not always meet with very wide reception among the consuming States.

Do you have any other suggestions as to what we should be looking at to provide that stability?

Mr. HURT. Mr. Williams, you so very eloquently pointed out the problems with trying to do an import tax and it looks like that with all the opposition in Congress, it would be very foolish for us to use our trading chips to try to achieve something of that nature. I think that we would be better served if we had at least some maintenance of our present tax incentives. We are dealing with the market situation as you say that we have no control over and if the producers had these tax incentives even though we feel the windfall profits tax is no comfort to us now, if we had something to look forward to in years to come when the economics do change where we could recoup some of the capital that we are losing now, I think it would give us an incentive to hang in there and keep trying to survive in this business.

Mr. WILLIAMS. Mr. Chairman, could I extend my remarks just to mention one thing which has caused some difficulties in the area which Congress I think can deal with and Mr. Hurt just mentioned. In terms of the windfall profits tax which is not a tax on profits, it is an excise tax. In terms of natural gas price regulation and all of its many categories I think 10 or 12 or 13 come to mind, and Mr. Perry is far more familiar with that, could probably add many more subcategories to it. One of the reasons that we had problems with OPEC II is that because in the United States we had price regulation on natural gas below market levels, below international market levels and we had price regulation on crude oil, that producers of both oil and gas did not have the same incentives here in the United States that they had elsewhere.

Had they had those incentives at the time of the Iranian Revolution, we would have been producing more oil and more gas than we were at that time and we would have been somewhat more insulated from that second round of price increases and instead of seeing a three-fold price increase in the 1979, 1980 or early 1981 period, we might have seen a much lower price increase both nationally and internationally. One of the things that distorted our local economy is when internationally prices went up 2½ times when you deregulated the price of crude, it went up 3½ times here.

And producers were insulated from information about international markets and did not go to the effort of understanding those international markets because they did not need to, they knew what prices were going to be, the government regulated it for us. We had that price stability but we were insulated from the knowledge of how the markets worked and so we became very narrow in our understanding of those markets and I think that that reduced

the potential production that we would have had at the time of OPEC II.

So, I think that while the import tax might be very difficult to impose, if you let us have free access to the markets that are out there, repeal the Field Use Tax Act, if you allow total deregulation of natural gas—I do not see any reason why it should be regulated—if there are emergency measures, you know let's do that Short Term Emergency Act to take care of them when they come out. But, there is more gas out there that cannot get to market because of current regulations, gas that these gentlemen are willing to sell and they are not allowed to because nobody will transport it. They do not have free access to the transportation system.

In other words, let us be free and that will add some price stability. It is not going to add total price stability, not nearly the kind of control you could get with an import tax but it will help the industry.

Mr. STENHOLM. There is no question about that. I was speaking to a group of dairy farmers in Columbus, OH last Monday and made reference to energy in my speech. I was confronted with a question asking what I meant by national energy policy. I gave basically the same answer you are giving; deregulation, allowing the market forces to function.

But then we come up to the next inevitable question. What happens when the prices go over the top because of unnatural market forces? Then where are we, the consumers? That is a challenge that we have to meet. Mr. Perry, you make a very excellent suggestion in the banking area in urging as to pursue parity and equity. If we are going to have one rule for the big banks to deal with bad oil loans in Mexico, then apply the same rules domestically. These arguments Larry Combest from Lubbock-Odessa, TX and Charlie Stenholm from Abilene, TX can make to our urban colleagues and have some credibility.

The problem that we have coming from the oil patch is a lack of credibility. We can predict, based on history, what is going to happen. There is going to be another shortage. The United States will become more vulnerable for our energy supplies and needs. If there is someone else who has one or two other very short suggestions, I would like to have them in the record at this time.

Mr. HOLLOMAN. We'd like to talk about tax incentives this morning. With \$6 and \$8 oil, tax incentives don't have much meaning because you must have profit before those things enter into the picture.

Mr. STENHOLM. You sound just like 100,000 farmers I have heard from, talking about agricultural policies. As long as there is no profit, it matters not what the policy really is.

Mr. HOLLOMAN. That is correct.

Mr. PERRY. Mr. Chairman, may I make one final statement about these tax policies? The drilling rig count peaked as of December 31, 1981 and in round figures, slightly less than 5,000 rigs. That probably was a distortion of what the real demand for drilling rigs should have been. It should probably have been more like 3,000 or 3,500. But if you will plot a curve of the drilling rigs vs. date and you find that tremendous peak—

Mr. STENHOLM. Drilling rigs vs.—

Mr. PERRY. Date. You will find this tremendous peak that occurred as of December 31, 1981, that also happens to be the date that the maximum tax rate was reduced from 70 percent to 50 percent. I am not here today to advocate for the benefit of the oil industry, the way we raised the maximum tax rate back up to 70 percent but I am here to tell you that these drastic changes that occur in maximum tax rate have had a significant impact on these gyrations we see in the drilling rig counts.

Now as a result of that, those people who buy and operate drilling rigs went out in the fall of 1981 and borrowed tremendous amounts of money and built additional rigs over and above what really were needed then. Now, they did not accurately perceive what the market really was but nevertheless, they did overextend in an attempt to respond to the demands and needs of this Nation at the time and the need was perceived to be the greatest.

We are talking about a change of maximum tax rate in a proposed flat tax or tax reform. It will have some additional impact on the drilling rig count if, as Mr. Holloman says, there is profit there. In other words, what will happen is on the effective date of change, those who are attempting to write off their intangibles will have a big drilling program in the end and we will see another hump in the drilling rig count in order to try to take advantage of the higher tax rate dollars for their drilling program.

If the price stays down around \$10 a barrel, I do not think you will see it occur because there is not enough profit in it. It does not really make that much difference. But the last, one of the things that Congress can do if we have a more uniform or make these changes less dramatic at the time and make them more over a period of time, it can soften the impact that it might have on the oil industry. Thank you, sir.

Mr. STENHOLM. Thank all of you for taking time to come and present this testimony to us today. If you have any additional information you would like to insert into the record, we will leave the record open 10 days from this point. Thank you all very much.

We will now hear from the second panel which consists of Dick Beveridge, Charlie McCoy, and Malcolm Abel. Let me welcome each of you. I recognize first Mr. Dick Beveridge, executive vice president of the Independent Petroleum Association of America, Midland, TX. Welcome, Mr. Beveridge.

**TESTIMONY OF DICK BEVERIDGE, EXECUTIVE VICE PRESIDENT,
INDEPENDENT PETROLEUM ASSOCIATION OF AMERICA, MID-
LAND, TX**

Mr. BEVERIDGE. Thank you, Mr. Chairman. I am Dick Beveridge, general partner of Western Reserves Oil Co., an independent oil and gas-producing company in Midland, TX. I am a member of the national executive committee for the Independent Petroleum Association of America. Our presentation includes information from 37 oil and gas associations representing all of the 33 producing States.

Our members generally only have one profit center, the sale of oil and gas at the wellhead. They also have only one principal activity for reinvestment of their income, exploration and development of new petroleum reserves. They do not refine, market, or

transport oil and natural gas as a principal business. It is obvious that our Nation is not soon going to replace oil and natural gas as our primary source of energy. Crude oil and natural gas, which now provide almost 70 percent of our total energy requirements, will be our primary energy source well into the next century.

Clearly, we have two choices. Either we can develop our own substantial domestic reserves or we can depend on foreign imports, depend on imports and place ourselves exactly in the posture we had at the time of the 1979 shortage. Our industry is now in the 5th year of a devastating economic shakeout. Since 1982, thousands of economic entities have been liquidated, thousands, including independent producers, drilling contractors, supply and equipment firms, and financial institutions. The end is nowhere to be seen and yet today we are under Government threat calling for even more tax revision for our industry.

Similar threats over past years have always led to punitive taxation. Today, outside investment has virtually stopped. And this investment is vital to our future. As of last week, our active, rotary rig count stood at 1,063 rigs. And I believe each of you has a chart reflecting active, rotary rigs for the past several years and the dramatic drop in 1986 has been highlighted. This is 23 percent as many rigs as were operating in December 1981. This collapse and essential activity, drilling activity, must be turned around.

At current levels of industry activity, by 1990 our import dependence will almost double or reach 60 percent of our Nation's daily requirements. If this occurs, we will again be at the mercy of OPEC both as to supplies and prices of essential energy and I think it would be good to note and to remember that our opponents in this country speak of a worldwide oil glut, well that oil glut does not exist in America. We have a shortage every day and we import almost 5 million barrels a day so we really need to remember that.

Our Nation is faced with a calamitous decline in current production as well as decline in exploration and drilling activity for future production so that today we have a significant threat to our national security. Recently the Interstate Oil Compact Commission estimated that at \$15 a barrel, as many as 100,000 stripper wells will be shut in within the next 12 months. In addition, many marginal wells not in the stripper category will also be prematurely abandoned.

If this happens, our production could fall by as much as 1 million barrels per day within 1 year. Drilling contractors are under severe strain. Most of them, if not all, are now operating close to the break even point or at a loss. Other service industries are simply shutting their doors. Tens of thousands of jobs are being lost. In February alone, our Labor Department reported 143,000 Texans were dropped from the work rolls; 143,000 is a pretty significant number and I can only hope that the Labor Department is not accurate.

Much of the expertise needed to find and produce oil and gas is being lost. It is tragic to see the young men and women who have been contributing their skills toward petroleum exploration and development being compelled to leave this industry and yet it is happening each day. These facts I believe demonstrate clearly three things. First, if we are going to avoid growing energy vulnerability,

our present level of drilling activity must be significantly increased. Second, the domestic petroleum industry is an economic basket case and it must be recognized. Our exploration and development programs are in a state of collapse. Third, our national interest is being placed in the hands of foreign, and sometimes unfriendly, nations. We simply must recognize this fact.

We must reverse current trends and restore exploration, drilling, and development activity to adequate levels. Over the years, Government has contributed to this situation by its past actions in continuous threats of negative action. The Government must be awakened to the conditions threatening both our short-term and long-term energy capability. Tens of thousands of marginal wells will be prematurely plugged and abandoned this year. We must hold this loss to a minimum. We must avoid increasing the power of foreign producers.

Mr. Chairman, we have a crisis of major proportion and it must be recognized. We recommend that the following be immediately adopted.

First, assure continued expensing of drilling costs.

Second, restore the percentage depletion for all domestic production and repeal the many unnecessary limitations on this percentage depletion.

Third, remove natural gas price controls and eliminate restrictions on the use and transportation of natural gas.

Fourth, terminate the windfall profits tax and I might add that today the windfall profits tax is a total zero and all we really have is a monumental bit of paperwork between the Government, the producers, the purchasers, the royalty owners, and everybody loses. It should be terminated immediately.

Fifth, revise banking regulations that are forcing banks to unnecessarily foreclose on struggling producers.

And, last, consider a refund to producers now operating marginal properties at a loss, some of the \$77 billion the Government denied these producers through the windfall tax.

These are just the most urgent of an extensive list of changes Congress should make. Congress must act to avoid the total collapse of the domestic exploration and production industry. And this appeal is not a ploy or a game where our industry hopes to get one or two of those six items, rather it's an urgent request for needed changes to help in this final hour of a struggle. And I believe it is a struggle our Nation's going to lose if Congress and the administration continue to refuse accepting the facts. Thank you for your attention.

[Mr. Beveridge's prepared statement, with attachments, follows:]

PREPARED STATEMENT OF DICK BEVERIDGE, EXECUTIVE
VICE PRESIDENT, INDEPENDENT PETROLEUM
ASSOCIATION OF AMERICA, MIDLAND, TX

INDEPENDENT PETROLEUM



ASSOCIATION OF AMERICA

AND

AMERICAN ASSOCIATION OF PETROLEUM
LANDMEN
ARKANSAS ROYALTY MEMBERSHIP
CALIFORNIA INDEPENDENT PRODUCERS
ASSOCIATION
COASTAL OIL AND GAS ASSOCIATION
EASTERN KANSAS OIL AND GAS
ASSOCIATION, INC.
EAST TEXAS PRODUCERS AND ROYALTY
OWNERS ASSOCIATION
ENERGY CONSUMERS AND PRODUCERS
ASSOCIATION
GEORGIA OIL AND GAS ASSOCIATION
ILLINOIS OIL AND GAS ASSOCIATION
INDEPENDENT OIL AND GAS ASSOCIATION
OF NEW YORK
INDEPENDENT OIL AND GAS ASSOCIATION
OF WEST VIRGINIA
INDEPENDENT OIL PRODUCERS TRI-STATE,
INC.
INDEPENDENT PETROLEUM ASSOCIATION
OF MOUNTAIN STATES
INDEPENDENT PETROLEUM ASSOCIATION
OF NEW MEXICO
INDIANA OIL AND GAS ASSOCIATION
KENTUCKY OIL AND GAS ASSOCIATION
LIAISON COMMITTEE OF COOPERATING
OIL AND GAS ASSOCIATIONS
LOUISIANA LANDOWNERS ASSOCIATION
INC.

LOUISIANA ASSOCIATION OF INDEPENDENT
PRODUCERS AND ROYALTY OWNERS
MICHIGAN OIL AND GAS ASSOCIATION
NATIONAL STRIPPER WELL ASSOCIATION
NEW YORK STATE OIL PRODUCERS
ASSOCIATION
NORTH TEXAS OIL AND GAS ASSOCIATION
OHIO OIL AND GAS ASSOCIATION
OKLAHOMA INDEPENDENT PETROLEUM
ASSOCIATION
ORANGE COUNTY PETROLEUM ASSOCIATION
PANHANDLE PRODUCERS AND ROYALTY
OWNERS ASSOCIATION
PENNSYLVANIA GRADE CRUDE OIL
ASSOCIATION
PENNSYLVANIA NATURAL GAS ASSOCIATES
PENNSYLVANIA OIL AND GAS ASSOCIATION
PERMIAN BASIN PETROLEUM ASSOCIATION
ROCKY MOUNTAIN OIL AND GAS
ASSOCIATION
ROYALTY OWNERS AND INDEPENDENT OIL
AND GAS PRODUCERS ASSOCIATION
OF ARKANSAS
TENNESSEE OIL AND GAS ASSOCIATION
TEXAS INDEPENDENT PRODUCERS AND
ROYALTY OWNERS ASSOCIATION
VIRGINIA OIL AND GAS ASSOCIATION
WEST CENTRAL TEXAS OIL AND GAS
ASSOCIATION

before the

UNITED STATES HOUSE

SUBCOMMITTEE ON ENERGY, ENVIRONMENT AND SAFETY

Hearings on Petroleum Industry Issues

April 1, 1986

I am Dick Beveridge, general partner of Western Reserves Oil Corporation, an independent oil and gas producing company in Midland, Texas. I hold a bachelor and master of science degrees in geology and have been a practicing petroleum geologist since 1954. I am appearing here as a member of the national Executive Committee of the Independent Petroleum Association of America. Together with thirty-seven unaffiliated state and regional associations listed on the cover page which join us in these comments, we represent essentially all of 12,000 independent oil and gas producers (and thousands of royalty owners) who account for 90 percent of all the wildcat drilling in the United States and 85 percent of all drilling, which results in finding a majority of the significant oil and gas discoveries. Our members generally have only one profit center -- the sale of oil and gas at the wellhead. They also have only one principle activity for reinvestment of their income -- exploration and development of new petroleum reserves. They do not refine, market or transport oil and natural gas as a principle business.

INTRODUCTION

In 1973, when we were all standing in gasoline lines, there was a great hew and cry from Congress, the Administration and the American public to do something about our energy problem. At that time, it was decided that we would

make the transition away from conventional fuels to alternatives, renewables, and exotic forms of energy. Conventional oil and gas would merely serve as a stop gap measure for a relatively short interim. It has since become obvious that we are not, any time in the reasonably near future, going to transition away from oil and natural gas as our primary sources of energy. Nuclear power has been stymied. The synfuels industry has collapsed. Development of coal is lagging due to transportation and environmental concerns. It is inescapable that crude oil and natural gas, which now provide almost 70% of our total energy, will be our primary energy sources well into the next century.

We have two choices. Either we can develop our very significant remaining reserves of crude oil and natural gas within the United States, or we can become dangerously overdependent on imported oil and place ourselves exactly in the posture we held at the time of the 1979 oil disruption. We have adequate reserves of oil and gas. What we don't have is the economic and regulatory framework necessary to develop those reserves. And it can't be done for nickles and dimes. It is going to require the commitment of unprecedented massive amounts of capital that will be invested only if Congress acts now to make the necessary changes in tax and regulatory provisions required to encourage people to invest in one of the most necessary, but still high risk, capital ventures an investor can undertake.

Our industry is now in the fifth year of a devastating economic shakeout. Since 1982, literally thousands of economic entities have been liquidated, including independent producers, drilling contractors, supply and equipment firms, and financial institutions. The principal oil producing states, whose government revenues are largely dependent on oil and gas prices and taxes, are confronted with monumental revenue shortfalls. And the end is nowhere to be seen.

Petroleum exploration and development always has been cyclical, but nothing in previous experience prepared us for the wild economic gyrations of recent

years. In the up-cycle from the mid-1970s through 1981, the industry expanded its activities at unprecedented costs covered by equally unprecedented debt obligations. Now, under threat of wholesale revision of historic energy tax provisions accompanied by precipitous declines in oil prices, many in the industry find their production costs, overhead, taxes and debt retirement requiring far more dollars than they are able to generate internally. Outside investment has stopped altogether.

As a result, we are witnessing the most dramatic and sustained "free fall" in domestic petroleum exploration and development in the entire history of the industry. The uncertainty created by pending tax legislation has been a principal contributing factor; it is not just coincidental that we are now operating just half as many drilling rigs as were running in December 1984, just after the Administration put forth its so-called "Treasury I" proposal which punitively would have eliminated all energy tax provisions imbedded in the economic fabric of our industry.

The chart, Rotary Rigs Active, shows our rig count as of March 24 at 1,063, only 23% as many rigs as were operating on December 31, 1981. Unless this collapse in essential drilling activity is somehow reversed, a perhaps irreversible decline in domestic petroleum production will soon be evident. At current levels of industry activity, our import dependence could almost double by 1991, from about 35% to some 60% of our requirements. If this occurs, we will again be at the mercy of OPEC both as to supplies and prices of essential energy.

Even before the collapse in crude oil prices over the past 90 days this industry was in economic difficulty. Now, our industry and the nation is faced with the prospect of such a calamitous decline in current production and the exploration and drilling activity necessary to maintain future production that there is already a significant threat to national security. Let me give you some details.

March 26, 1986

	(Thous. b/d)	Four-Week Moving Average Ending:			Vs. Year Ago	
		MAR. 7	MAR. 14	MAR. 21	Units	%
TOTAL DEMAND	Motor Gasoline	6,827	6,960*	7,062	465	7.0
	Aviation Fuels	1,329	1,367*	1,441	170	13.2
	Middle Distillates	3,768	3,865*	3,766	392	11.6
	Residual Fuel Oil	1,640	1,628	1,560	-65	-4.0
	All Other	3,200*	3,850*	3,800	-95	-2.4
	GRAND DEMAND	17,524*	17,621*	17,625	667	3.8
TOTAL SUPPLY	Production:					
	Districts I-IV	5,864	5,879	5,894	-43	-0.7
	District V	3,070	3,065	3,060	47	1.6
	Crude Oil Production	8,933	8,944	8,954	5	0.1
	NGL Production	1,618	1,636	1,654	-29	-1.7
	GRAND PRODUCTION	10,553	10,580	10,558	-24	-0.2
	Imports:					
	Crude Oil	2,924	3,057	2,912	368	14.5
	Motor Gasoline	453	374	338	-54	-13.8
	Aviation Fuels	61	65	75	43	134.4
REFINING	Middle Distillates	91	123	155	-16	-9.4
	Residual Fuel Oil	516	655	579	-34	-5.5
	All Other	592	597	601	62	11.5
	GRAND IMPORTS	4,207	4,872	4,683	368	9.6
	Other Supply	980	1,048	1,125	360	47.1
	TOTAL SUPPLY	16,337	16,498	16,372	704	4.5
STOCKS (Thous. Bbls.)	Motor Gasoline	240,171	236,056*	227,295	7,202	3.3
	Aviation Fuels	46,514	48,005*	48,302	4,809	11.1
	Middle Distillates	117,422	110,912*	106,766	-9,135	-7.9
	Residual Fuel Oil	41,249	40,888	40,224	-6,119	-13.2
	Other Products	108,000	106,000	100,000	-40,000	-28.6
	TOTAL FINISHED STOCKS	554,073	524,961*	522,587	-43,144	-7.6
	Unfinished Oil & NGL	110,593	109,323*	108,783	-4,369	-4.4
	Crude Oil	337,119	336,360*	336,234	2,026	0.6
	TOTAL STOCKS	1,001,785	970,644*	967,604	-46,087	-4.5
WHOLESALE PRICES	Unleaded Gasoline (\$/Gal)	43.71 ¢	42.93 ¢	44.15 ¢	-18.00	-46.3
	Kerosene (\$/Gal)	51.95 ¢	52.15 ¢	53.67 ¢	-28.18	-24.4
	Distillate Fuel (\$/Gal)	47.05 ¢	47.29 ¢	48.77 ¢	-28.02	-26.5
	Residual Fuel (\$/Gal)	40.62 ¢	40.39 ¢	39.91 ¢	-19.39	-32.7
	Avg. 4 Products (\$/Gal)	43.72 ¢	43.22 ¢	44.05 ¢	-10.43	-40.9
	Avg. 4 Products (\$/Bbl)	\$18.36	\$18.18	\$18.50	-12.78	-40.9
WELLHEAD PRICE	Unleaded Gasoline (\$/Bbl)	\$18.50	\$17.00	\$18.50	-8.75	-39.4
	Unleaded Gasoline (\$/Gal)	39.92 ¢	35.81 ¢	39.50 ¢	-19.96	-17.6

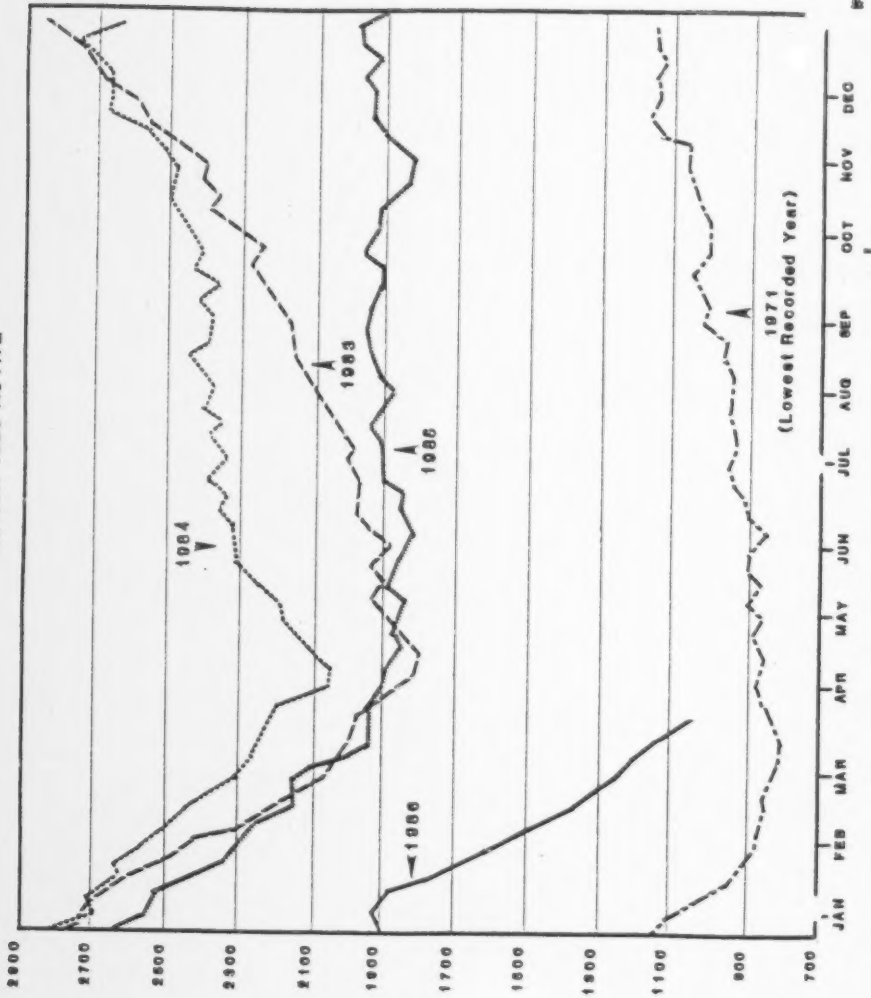
NOTES: Other supply includes net processing gain, unaccounted for crude oil and other hydrocarbons. Retail price of unleaded gasoline includes tax. SPR imports and stocks excluded.

SOURCES: Supply, demand, stocks and refining figures based on weekly data published by the American Petroleum Institute; rotary rigs from Hughes Tool Company; wholesale prices based on low quotes from Platt's Oilgram Price Report and retail gasoline price from Oil & Gas Journal.

CONTACT: IPAA Statistics Department

* Revised data

ROTARY RIGS ACTIVE



Hughes Rotary Rig Count
1985-1986

	Week #	1985	1986
January	1	2,576	1,915
	2	2,556	1,880
	3	2,453	1,773
	4	2,370	1,671
February	5	2,303	1,594
	6	2,271	1,496
	7	2,175	1,376
	8	2,162	1,308
March	9	2,143	1,248
	10	2,011	1,212
	11	1,934	1,137
	12	1,937	1,063
April	13	1,939	
	14	1,910	
	15	1,898	
	16	1,860	
May	17	1,862	
	18	1,855	
	19	1,841	
	20	1,901	
June	21	1,869	
	22	1,848	
	23	1,821	
	24	1,851	
	25	1,854	
	26	1,907	

	Week #	1985	1986
July	27	1,904	
	28	1,910	
	29	1,931	
	30	1,908	
August	31	1,890	
	32	1,911	
	33	1,928	
	34	1,945	
September	35	1,940	
	36	1,932	
	37	1,917	
	38	1,912	
October	39	1,955	
	40	1,935	
	41	1,934	
	42	1,906	
November	43	1,839	
	44	1,838	
	45	1,864	
	46	1,895	
December	47	1,942	
	48	1,946	
	49	1,962	
	50	1,911	
	51	1,983	
	52	1,995	
	53	1,898	

te: The monthly designations apply to 1986 data only.

IPAA

SHORT TERM IMPLICATIONS

A massive drilling effort in the period 1973-1981 reversed the decline in U.S. petroleum production. This reduced our dependence on imported petroleum from 46 percent in 1977 to 30 percent in 1985. Now that situation is being reversed, with domestic production declining and imports increasing.

The short term production decline is directly related to reduced cash flow caused by rapidly declining crude oil prices and negative tax treatment of producers. The drop in production could reach 1,000,000 barrels per day within a year. Additional production declines will result in the future due to failure to drill new wells to replace the normal 10 percent per year production decline in wells still in production.

A producer can operate a well until it doesn't yield any cash flow, i.e., the current operating costs equal the current revenue from the sale of crude oil. If the producer has a reasonable expectation that within a short time -- two or three months -- revenues will increase or costs can be reduced; production may be continued at a loss. However, most producers, and especially smaller independents, are so hard pressed for cash flow that there is almost no leeway for making the decision to cease production. Once this occurs, it is very unlikely production will ever be resumed.

Most oil and gas leases provide that if production from a property ceases for sixty days (other than for normal maintenance or a "workover" of a well) the lease is automatically terminated. Also, most states have regulations that require a well to be physically "plugged" by injection of cement into the well bore under stringent environmental protection procedures, usually within 90 days after production is halted. The relatively low volume of production and remaining reserves make the cost of drilling a new well prohibitive unless the price increases several fold. The Texas Railroad Commission recently modified plugging requirements on a temporary emergency basis to extend the time to one

year. This will certainly help, but many wells will still have to be plugged, even in Texas and it doesn't change requirements in other states.

The National Stripper Well Association and Interstate Oil Compact Commission estimate that 100,000 stripper wells will be shut in within a year. There are an estimated 465,000 wells in the stripper class, 72 percent of all producing wells. In 1985, these wells produced an average of 2.74 barrels of oil totalling 1.3 million barrels per day, or about 15 percent of all the oil in the U.S. or 17% of the oil produced in the Lower 48. Majors and independents each produce about half of the stripper oil but the larger companies must have higher volume wells to be economic. It is estimated that independents operate 331,000 of the stripper wells, more than 71 percent. If 100,000 of the stripper wells are shut in, 270,000 barrels per day of total production will be lost.

However, wells not in the stripper class will also be plugged. Excluding both North Slope wells and stripper wells average production is 33.4 barrels per well per day. A certain number are high volume producers. If 25,000 of those wells average 100 barrels per day, then the remaining 15,600 average about 22.7 barrels per day. If 10 percent of the latter wells are shut in, then an additional 355,000 barrels per day of production will be lost.

Total lost production would be about 530,000 barrels per day.

In addition to this lost production, the remaining production will have a normal decline of about 10 percent.

If we complete 19,000 new oil wells each adding an average production of 20 barrels per day, about 400 barrels per day will be added. Balancing the lost production with new production indicates that daily production could fall as much as one million barrels within one year. This analysis assumed a price no lower than \$15 per barrel. Since prices are well below that now, the potential loss of production is frightening to contemplate.

Drilling contractors are under severe strain. Most are operating close to a cash break even point and further reductions in cost are almost impossible. If the contractor has debt against the rigs, he will probably go under. Others will go out of the business by "mothballing."

Other service companies will just shut their doors or streamline their already streamlined operations with an attendant loss of jobs.

It is estimated that with each \$1 per barrel drop in oil prices, 25,000 jobs are lost due to decreased petroleum industry activity.

Many banks will be hard pressed to avoid problems. Although a great many reworked their loan portfolios over the last several years and made new loans based on \$15 oil on 50 percent of the estimated reserves, these limits have been reached. If a bank has not restructured in that fashion, it may already be in a problem position. One problem the banks have is the state or federal regulatory agencies pushing them to impossible positions, given the circumstances, in the guise of protecting the depositors when in fact the opposite tactic might be more beneficial.

From a total expenditure for exploration and development of \$56.475 billion in 1981, the industry probably spent about \$35 billion in 1985. A drop to \$20-25 billion could occur in 1986. If the rotary rig count averages 1,200 for the year (highly unlikely), at a rate of 38 wells per rig 45,000 wells could be drilled compared to 76,000 in 1985. The long-term implications are frightening.

LONG RANGE IMPLICATIONS

One of the constants in the history of the oil industry has been its consistent record of being sold short, by persons in and out of the political community. Domestic crude oil production peaked at 9.6 million barrels daily in 1970 then declined over a six year period to 8.1 million barrels daily, a loss of 1.5 million barrels daily. There were few who predicted that this

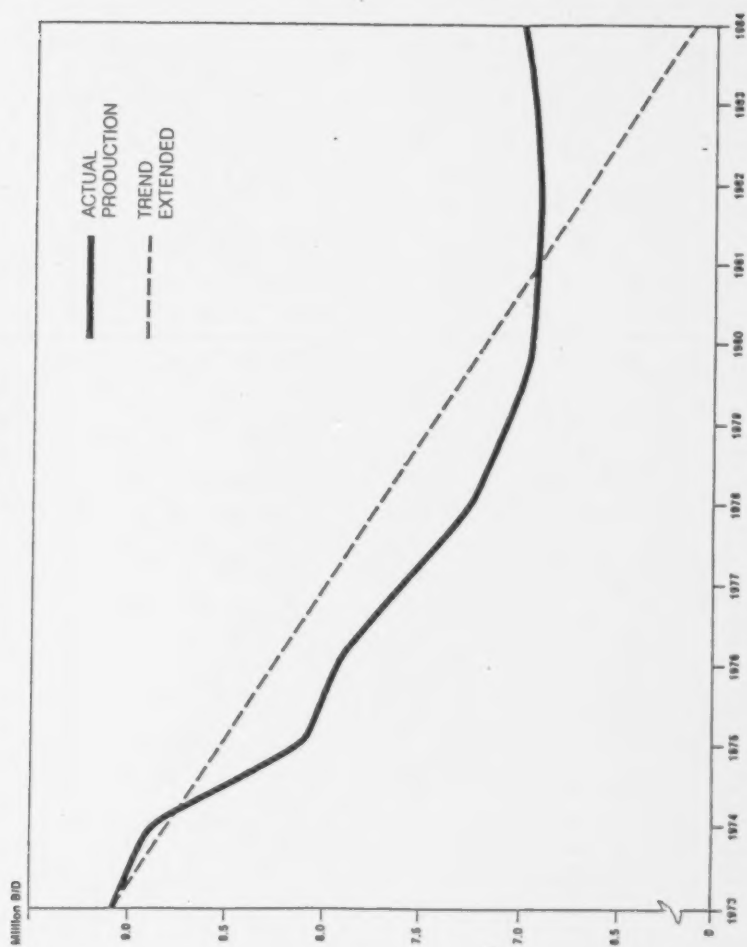
decline could have been arrested and even increased somewhat in the past five years. Chart 2 compares actual production with the trend line of the 1970-77 experience. The stabilization of domestic production was achieved by extraordinary efforts by independent producers, involving the drilling of 202,652 new oil and gas wells in the six years ending in 1984 -- 155 percent more than was drilled in the six years following the peak production year of 1970. But this 166 percent gain in drilling was achieved at a cost of \$299 billion -- an increase of 419 percent over the 1970-76 period.

While these extraordinary efforts halted the production decline, few recognize the significance of this in terms of balance of payments savings, and of helping to reduce OPEC's control over both markets and prices. Except for this increased oil drilling, U.S. production would have been 1.3 million barrels per day less in 1984, and our additional costs for imported oil would have been almost \$15 billion greater.

The dominant force in not only stabilizing production, but in raising the daily output by about 300,000 barrels since 1979, is attributable to the multiplicity of efforts by independent producers. In this same period, the combined lower 48 production by the 25 or so larger companies identified as the "Chase Bank Group," actually has declined by 300,000 barrels daily. In arresting the production decline, independents have offset this production drop experienced by the major companies. As a result, the share of lower 48 production by independents has increased from 29 percent 10 years ago to about 40 percent today.

RESPONSE TO DRILLING EFFORT

Crude Oil Production

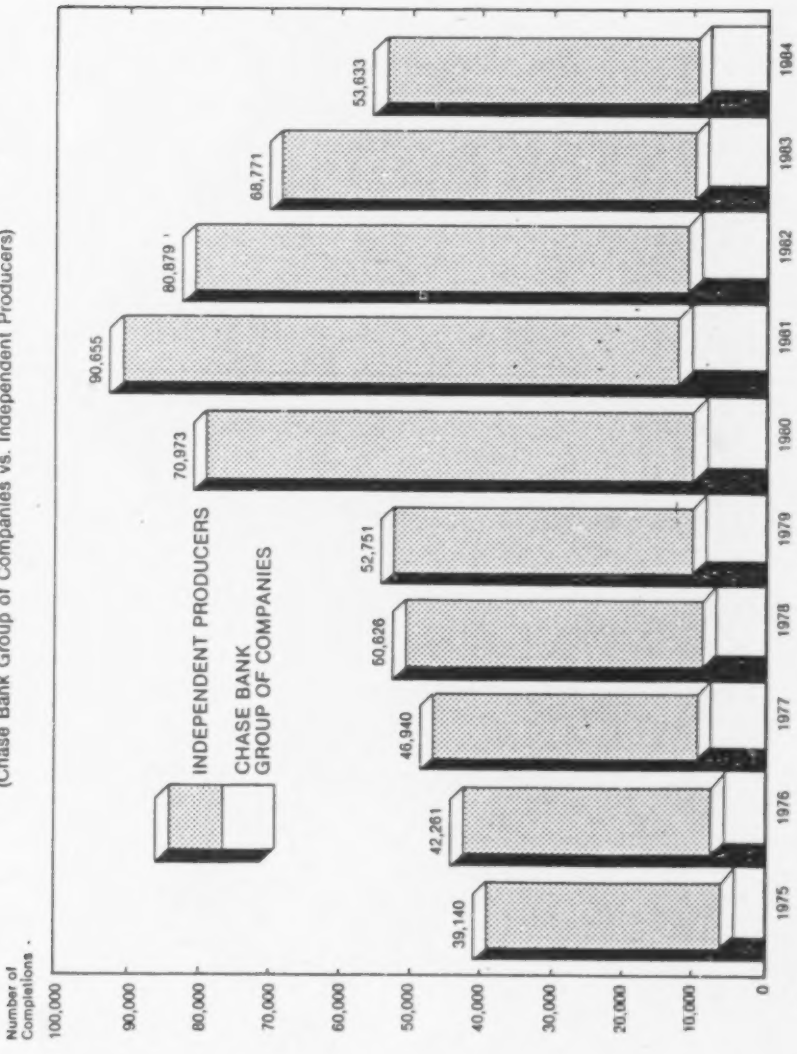


Source: DOE/EIA (Data for lower 48 states)

IPAA Chart 2
June 1985

Chart 3 shows the dominant role of independents in domestic exploration/development. They have accounted for 87.3 percent of total well completions in the past 10 years; or 550,185 wells out of 629,825 drilled. In the past 15 years, the U.S. has found as much oil as it produced in only one year, 1981. As can be seen, total drilling as reported to date has dropped sharply in the past three years, with 56,633 total wells reported for 1984 representing only 62 percent of the 1981 well completions.

CHART 3
TOTAL WELL COMPLETIONS IN THE U.S.
 (Chase Bank Group of Companies vs. Independent Producers)



Source: Petroleum Information, Inc.

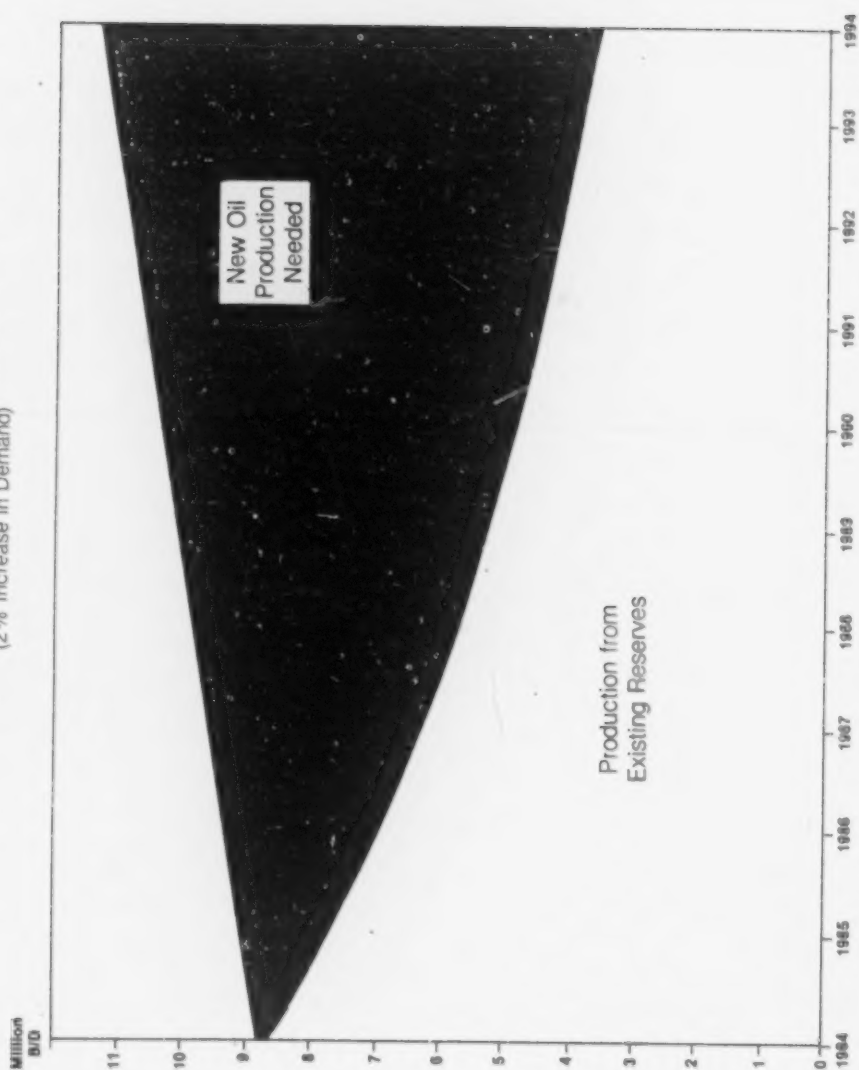
IPAA CH
 MARCH 1985

Energy vulnerability means different things to different people. Some view the question only in terms of military security. Our nation has never had a fuel problem in a military emergency, however. While adequate energy supplies are important to military security, they are equally important for the transportation, employment and economic security of the American people. We learned this lesson in the 1970s during imposed shortages of petroleum liquids, as well as artificial natural gas shortages which resulted in plant and office closings and unscheduled, unpaid "vacations" for Americans in many sections of the country. We should not forget these experiences, and it should be national policy to minimize the chance that they will occur again.

If the nation is to have relative energy security, which I would define as the ability to cope with significant import supply disruptions with no substantial or lasting impairment of economic activity, there is no question that current exploration/development drilling will have to be significantly increased. Chart 4 projects the production which must be found and developed if we are to contain import dependence at the current level of about 30 percent of domestic demand. (This projection assumes an increase in demand of only two percent in the period 1985-94, which is below the growth we are experiencing currently. The World Bank estimates that a 25 percent drop in petroleum prices below \$25 per barrel will increase demand 5 percent over two years and 10 percent within five years. Prices have already declined at least 40% below \$25.)

As can be seen, domestic production will have to be increased by 11.4 million barrels daily by 1994. Because of the natural production decline from existing wells, this means 13 million barrels of new daily production will be required in this period.

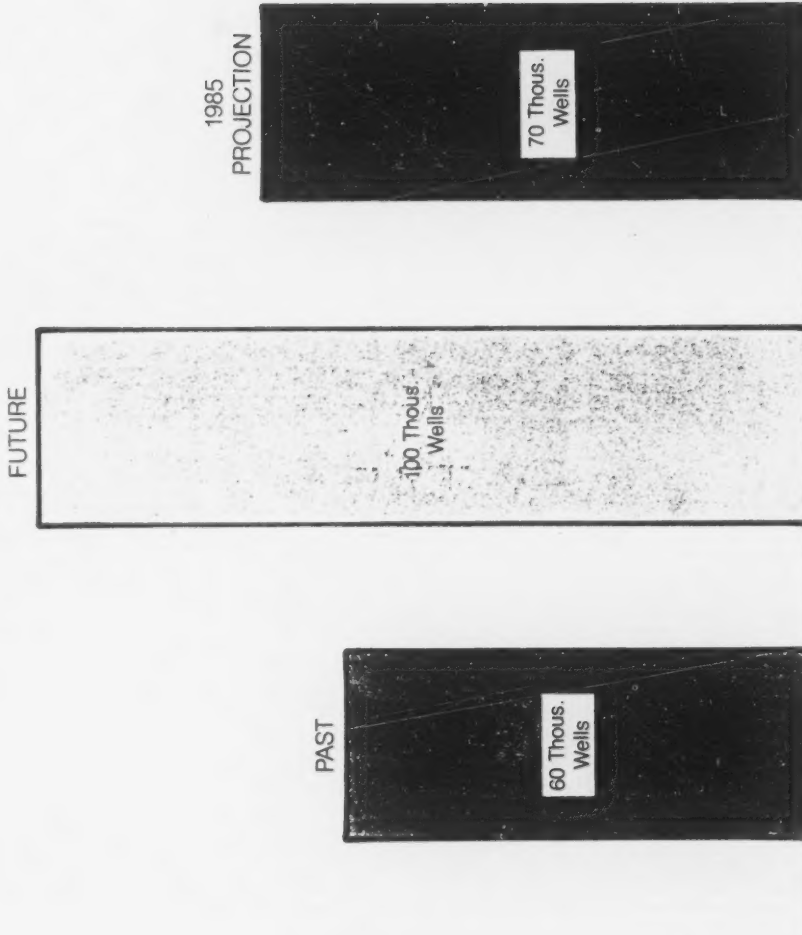
NEW CRUDE OIL PRODUCTION NEEDED (2% Increase in Demand)



IPAA Chart 4
June 1985

Now, let us look at the drilling requirements to achieve this essential growth. Charts 5 and 6 illustrate that to meet 70 percent of domestic demand for petroleum liquids from domestic resources in the coming decade, the industry will be required to spend \$620 billion and drill a total of 1,000,000 new wells. Maintaining relative energy security, in other words, will require a commitment of unprecedented capital resources to drill unprecedented numbers of wells.

DRILLING REQUIREMENTS 10 Year Average

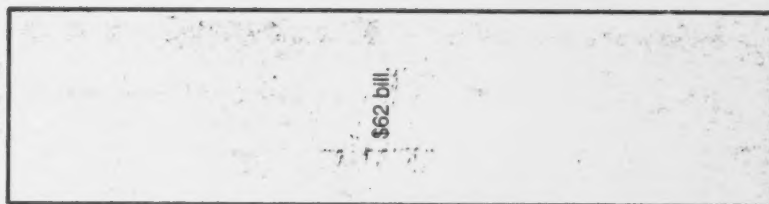


Source: API, IPAA

IPAA Chart 5
June 1985

EXPENDITURE REQUIREMENTS
10 Year Average

FUTURE



PAST



\$32 bill.

1985
PROJECTION



\$35 bill.

How does the activity level of the industry stack up against these requirements?

Just since mid-December 1984, the number of rotary rigs at work has dropped by 1,724 units or 62 percent. As of today, 76 percent of the industry's operable rotary rig fleet is idle. These facts clearly illustrate that while the economy as a whole is in its third year of recovery, the petroleum exploration/producing industry remains in a downcycle that shows no signs of abating. Recent experiences of the domestic industry have been marked by numerous sales, mergers and bankruptcies, continued difficulties in a number of oil country banks and extreme financial difficulties among a multiplicity of long-established organizations providing equipment, supplies and services to the industry.

The preceding facts, I believe, demonstrate clearly that (1) if we are to avoid growing energy vulnerability, our present level of drilling activity must be quadrupled, (2) the domestic petroleum industry virtually is an economic "basket case" with its exploration/development programs in a state of collapse and (3) the public and the national interests will be ill-served unless we can reverse current trends and restore exploration/drilling/development activity to adequate levels.

CONCLUSION

Government has contributed to this situation by its past actions and threats of negative actions. Government has to be concerned about conditions threatening both our relatively short-term and long-term energy producing capability, and there are things that Government can and must do if our industry is to be effective and aid in our country's continued progress and economic well being.

We are already confronted with the certainty that tens of thousands of marginal or stripper wells will be plugged and abandoned this year because of

the precipitous drop in oil prices. Each barrel of daily production lost will have to be replaced by a barrel of imported oil. Also, hundreds of millions of barrels of potential future reserves will be lost forever. To hold that loss to a minimum and avoid increasing the power of OPEC, we urge:

- (1) Assure continued expensing of intangible drilling costs in the year expended or incurred and modify the definition to include geological and geophysical costs and unrecoverable surface casing.
- (2) Restore percentage depletion for all domestic oil and gas production and repeal the 50 percent of net income and 65 percent of taxable income limitations and remove the restrictions on transfers of proven properties.
- (3) Repeal the Windfall Profit Tax.
- (4) Remove natural gas wellhead price controls.
- (5) Eliminate restrictions on the use and transportation of natural gas.
- (6) Revise certain rules of the FDIC, the Comptroller of the Currency and the Federal Reserve Board that detrimentally affect the oil and gas industry.
- (7) Immediate adoption of a marginal well Production Maintenance provision to assure continuation, until the market stabilizes, of production from properties which otherwise would be abandoned.
- (8) Ease certain environmental restrictions related to underground injection control (UIC) and speed efforts by EPA for approval of state UIC programs.

These are just the most urgent of an extensive list of positive changes Congress can make to help avoid the total collapse of the domestic petroleum exploration and production industry as we know it today. A more complete list is attached as an exhibit.

Thank you.

IPAA ENERGY ACTION RECOMMENDATIONS

A. TAX ISSUES

For Maintenance of Existing Production:

- o Restore percentage depletion for all production at 27 1/2%, and
 - Repeal 50% of net income per property limitation
 - Repeal the proven property transfer rules
 - Repeal the 65% of taxable income limitation per taxpayer
- o Repeal windfall profit tax: until then, repeal WPT proven property transfer limitations
- o Ensure that the "once a stripper, always a stripper" rule is kept intact
- o Repeal IDC recapture rules or revise to delete reference to percentage depletion in calculation of recapture offset
- o To prevent the premature plugging and abandoning of wells currently operating below the breakeven point adopt a marginal well production provision using a mechanism to refund WPT previously paid.

To Encourage New Exploration and Development:

- o Retain full deductibility of IDC and percentage depletion for all producers
- o Retain ACRS depreciation and the Investment Tax Credit
- o Treat geological and geophysical costs and unrecoverable surface casing as IDC
- o Provide an Exploratory Tax Credit of 15% of expenditures for exploration activity
- o Remove restrictions on the deductibility of IDC payments made pursuant to carried interest arrangements
- o Extend the 90-day economic performance rule for prepaid IDC when state frost laws apply
- o Revise the economic performance rules to permit accrual basis taxpayers a deduction for prepayments of IDC
- o Repeal Revenue Ruling 77-176 concerning deemed income resulting from acreage earned outside of the drill site
- o Repeal Revenue Ruling 83-46, which reverses a long standing IRS interpretation of the pool of capital doctrine
- o Reinstate the at-risk aggregation rules for oil and gas properties

Alternative Minimum Tax:

- o Maintenance of the current law net income offset for excess IDC
- o Maintenance of the AMT rate at less than 50% of the regular tax rate
- o Codification of tax benefit principles which ensure that the percentage depletion deduction will not be permanently lost due to the AMT
- o Extend the provisions of H.R. 3838 regarding treatment of farmers under the AMT to insolvent oil and gas producers

B. REGULATORY ISSUES

Natural Gas Recommendations

- o Repeal the Fuel Use Act
- o Deregulate natural gas
- o Provide for the non-discriminatory carriage of natural gas

Banking Recommendations

- o Modify existing regulatory requirements as follows:
 - Lengthen the period banks can amortize energy loans and reschedule repayments
 - Modify legal "net worth" guidelines for energy lender banks

C. ENVIRONMENTAL ISSUES

- o Streamline the Underground Injection Control (UIC) program to:
 - Expedite EPA approval of state UIC programs
 - Expedite permit approvals in states with EPA run programs
 - Modify the UIC program substantive requirements such as mechanical integrity testing to include less costly alternatives

Public Land Recommendations

- o Retain the Simultaneous Oil and Gas Leasing System
- o Extend lease terms on existing onshore and offshore public lands
- o Discourage any land use restrictions such as additional unnecessary environmental requirements or land withdrawals
- o Maintain the currently scheduled offshore lease sales
- o Suspend the proposed BLM/FS land exchange

Mr. STENHOLM. Thank you, Mr. Beveridge. Next we will hear from Mr. Charlie McCoy, president, Permian Production Equipment Co., Midland, TX, representing the Permian Basin Petroleum Association. Mr. McCoy.

**TESTIMONY OF CHARLIE McCOY, PRESIDENT, PERMIAN
PRODUCTION EQUIPMENT, INC., MIDLAND, TX**

Mr. McCoy. Mr. Chairman, members of the committee, thank you for the opportunity to appear before you today. I am Charlie McCoy, an executive committee member of the Permian Basin Petroleum Association and president of a small, privately owned company in Midland, TX, which serves a petroleum industry.

The Permian Basin Petroleum Association has 1,500 members composed mainly of small independent oil and gas producers and related service and supply managers who represent a work force of over 30,000 people. The Permian Basin is the largest single crude oil producing region in the lower 48 States both in size and in barrels of production. It encompasses 54 counties in west Texas and four counties in eastern New Mexico, or about 100,000 square miles, and produces over 20 percent of the Nation's total crude oil.

The independent producers and supporting oilfield service and supply companies have been hurt and will suffer further hardships from the effects of tax reform proposals which threaten to reduce or eliminate intangible drilling costs, depletion allowables, investment tax credits, and other provisions which enable those engaged in exploration drilling and production to maintain a workable cash-flow for investment into a high-risk and unstable industry.

Disregarding the 50-percent reduction in crude prices since the year's beginning, the tax reform threat has caused a decline in just about every oil and gas business statistic in the basin. The rig count, which is the direct indicator of area drilling activity and supporting jobs, has fallen from 509 from 1981, to 365 in 1985, to 295 in January 1986. And today, because of the added detrimental effects of low crude prices, the rig count is 176. We have had a 44-percent decrease in working rigs since the first of the year of Permian Basin.

The infection of the drilling activity decline has spread to most other businesses. In the Permian Basin, oil and gas revenues have fallen from a high of \$1.93 billion in 1981 to \$1.38 billion in December 1985. Even when a barrel of oil was still worth \$28, exploratory wells drilled from January through October 1985 were down 30 percent from the peak of 1982, because investors routed their dollars elsewhere where risks were limited, profits were stable, and the threat of tax reforms did not threaten their investment incentives.

The Permian Basin Petroleum Association has joined hundreds of other associations and businesses in telling the Congress in America that tax reform was the wrong bill at the wrong time and that it in no way represented the original intent of the bill. Even the majority of our congressional Members admitted that the bill was poor and that our priorities should be devoted to solving our deficit problems but regardless, a bad bill was passed due to Presi-

dential pressure with the false hope of a cleaning up by the Senate or a veto by the President.

Commendably, the people of west Texas remain optimistic. While bankruptcies and FDIC takeovers abounded, most businesses believed this was just another slump in a historically unstable industry and that if we could just hang in there a bit longer, we would survive and see a more promising future. Now, along with tax reform has come the drastic decline in crude prices. From \$28 a barrel in December 1985, our crude now sells for \$14 to \$17. I think we had a new quote this morning since this writing.

Marginal producing wells such as strippers, which produce less than 10 barrels a day, will be plugged because expenses have now far exceeded the revenues. It is estimated that approximately 170,000 low-volume or marginal wells have already become uneconomical to produce. I personally visited with numerous oil operators in the past month, both majors and independents. They have expressed their concern over the number of wells in their operation that fall into this category. Those operators estimate that the average well in this category has over 12,000 barrels of oil to be produced over the remaining life of their wells. For 170,000 wells, this amounts to 2.2 billion barrels of oil already found under production that will be lost unless steps can be taken to support oil prices so it will be economically feasible to produce these wells.

Approximately 637 million barrels of that oil is in the Permian Basin. To replace these reserves with new oil finds would cost the industry approximately \$25 billion using a \$12 per barrel cost and with the present trend of the industry with incentives to invest in drilling programs withdrawn through tax reform, this will simply increase our dependence on foreign oil and increase our trade deficit even more. The service companies, such as those engaged in drilling muds, chemicals, workovers, wire line services, seismic, drilling supplies and bits, pipe outlets, production equipment manufacturers, and hundreds of others who provide a service to the oil patch are fearing the bite of tax reform and low crude prices even more so.

My company, Permian Production Equipment, Inc., is a manufacturer and distributor of oilfield production equipment. Our business was progressing at a steady pace. We were purchasing shop equipment, training new people, even expanding to other market areas. Then came tax reform uncertainty, suspicion settled over the energy industry, projects were canceled, drilling programs curtailed, secondary recovery projects put on the back burner. The industry began to suffer.

There was still no answer from Washington on tax reform; however, we increased our efforts, cut costs where possible, and leveled off at a survival status cash-flow. Now, the energy industry has been dealt yet another blow. The price of crude has fallen to within a few dollars of what it cost to explore and find domestic oil. New exploration has virtually come to a halt. The only drilling activity today is development drilling. Every service and supply company, large or small, is having severe problems, some are in chapter 11, some are headed that way, and a large number of the smaller entities are already gone.

This Nation is losing its domestic oil and gas industry and what is even worse, with all the energy-related layoffs, we are losing our most valuable asset, the people who make up this industry. We are becoming more dependent on foreign energy every day. Over half of our foreign trade deficit is due to oil imports and such importation will increase because our reserves are being depleted at a rate of 15 percent per year without replenishment. So without a healthy, domestic energy policy, we will again be at the mercy of foreign governments for our needed energy requirements, some of which cannot be considered as our allies.

A man in the oil and gas industry today reminds me of the man that fell over a cliff, tax reform. On the way down he grabs onto a branch and stops his fall, he looks up from where he has fallen and cries out for help: "Is there anybody up there that can help me?" And there is Washington. Washington says: "Not to fear, tax reform is revenue neutral, the economy is on the upswing, unemployment is on the decline, trust me. Turn loose and I will help you." The man looks back up and cries: "Is there anybody else up there?"

Thank you, Mr. Chairman.

Mr. STENHOLM. Thank you, Mr. McCoy. Next we will hear from Mr. Malcolm D. Abel, vice chairman, National Energy Policy Committee from the Texas Independent Producers & Royalty Owners Association [TIPRO], Austin. Welcome, Mr. Abel.

TESTIMONY OF MALCOLM D. ABEL, VICE CHAIRMAN, NATIONAL ENERGY POLICY COMMITTEE, TEXAS INDEPENDENT PRODUCERS & ROYALTY OWNERS ASSOCIATION [TIPRO], AUSTIN, TX

Mr. ABEL. Mr. Chairman, Congressman Combest, thank you very much for the opportunity and privilege to appear here today. I am Malcolm Abel, an independent petroleum producer residing in Midland, TX. I appear here today as vice chairman of the National Energy Policy Committee of TIPRO. TIPRO is composed of more than 5,000 members who have an interest in oil and gas in the State of Texas.

The independent producers and royalty owners are the small business elements of the domestic oil and gas producing industry. The independents are specialists drilling over 85 percent of the Nation's wells and maintaining production on most of the marginal well properties that average less than 10 barrels of oil per day or less than 60 Mcf of natural gas per day. Their dual function of looking for new reserves and preserving production from old and declining reserves is vital to the Nation's economic and security objectives.

TIPRO members share the concern of all Texans over the present economic conditions in our State and we are particularly concerned with the adverse impact the falling crude oil and natural gas prices will have on the infrastructure of the domestic energy producing sector upon which our State and Nation depend. Today, our Nation faces the prospects of rising imports, increasing consumer demand, and declining activity of oil and gas exploration and production. We are once again facing a dangerous situation of overdependence on imports to supply our energy needs.

TIPRO would welcome any remedial relief by Congress to help assure that the domestic industry can continue to serve the nation's economic and strategic security objectives through maximization of domestic oil and gas recovery. We continue to believe that an oil import fee system is the only workable medicine for our industry's illness caused by artificially low oil and oil product prices. It is a remedial measure that if structured properly, could serve positively the economic and strategic well being of our Nation.

America needs a sound energy policy, a policy that encourages a strong domestic oil and gas industry in order to minimize the threat to our national security created by unacceptable levels of imported petroleum products from often unstable foreign governments. While this energy policy should certainly include enhanced incentives for exploration and drilling in the income tax code, elimination of the windfall profits tax, deregulation of natural gas prices, and a revamping of the FDIC regulations on energy loans, an oil import fee is urgently needed to insure that a stable supply of domestically produced oil and gas remains the foundation for satisfying our Nation's vital and fundamental need for energy.

I am not talking about a goal of energy independence but the need for a national energy policy. The United States is going to import some portion of its oil needs in the foreseeable future but this amount should not increase just because certain nations are currently dumping crude oil and crude oil imports onto the world market causing the price to fall so quickly that the domestic industry has no economic choice but to stop drilling important programs.

An import fee should be a temporary measure that can be used to counter the dumping of cheap foreign oil and refined products on the world market by countries that control the surface supply and that are currently participating in a strategy to increase production in an effort to discipline other oil exporting nations. Such a tariff system should not be a windfall for independent domestic producers but a measure designed to help them survive while at the same time shifting to foreign producers part of the cost burden of maintaining import flow into the United States. Both domestic producers and consumers should be protected from the extreme fluctuations in world oil market created by the whims of nations that would undermine our goal of insuring a consistent supply of adequate and affordable energy.

The imposition in the 1970's of the windfall profits tax on domestic producers and not foreign producers brought no cries from the economists that such was tampering with the free market system. Likewise, the imposition of an import tax should not be considered as interfering with the free market system. First of all, I doubt that anybody really believes that what is going on in the world oil markets today is a free market. It is unfair to let American consumers believe that we can continue very long having an adequate supply of energy at less than replacement cost.

TIPRO believes that an effective import fee should be free from exceptions that would cause bureaucratic complexity and inadequate control of imported crude oil or product volume. The fee should be variable in nature, come into existence only when prices fall below prescribed levels. In this way, the fee would not cause undue increase in oil cost to the consumer while at the same time

assuring the domestic producing industry economic opportunity to maintain vital exploration and development activity.

Such a system should minimize problems for exporting industries in that the fee would be temporary in nature and would be applied only at modest pricing levels. Should the need arise to assist selected exporting countries that are adversely impacted by an import fee, TIPRO believes this could be done in many ways other than through disrupting exemptions to the import fee application.

Since anticipated pricing patterns for petroleum threaten the very existence of a substantial portion of our domestic producing industry, our association believes a modest sacrifice by all to sustain an import fee system may be in the best long range interest of the Nation. For the foreseeable future, a viable domestic industry is needed to maintain the core supply of oil and gas required to keep demand for foreign supply a workable minimum. The alternative is serious overreliance on foreign supply which may prove to be insecure and extremely expensive in the long run.

TIPRO sincerely hopes that members of this committee will join with other Members of Congress in support of a viable import fee system. Oil and natural gas prices are continuing to decline to levels that will not sustain a healthy domestic industry. We see no other solution to this problem that will work in the short time still available to us.

Thank you for the opportunity to testify today.

Mr. STENHOLM. Thank you, Mr. Abel. Mr. Combest.

Mr. COMBEST. Thank you, Mr. Chairman. Gentlemen, I again would like to compliment you on your testimony and on the specific facts that you are giving us; those are very, very helpful. I guess we are sort of preaching to the choir, if I may use that adage, because I think among the producing States, you will find an overwhelming, at least a significant majority, of those of us in Congress that are going to support pretty much line item by line item what it is that you are proposing.

Some legislation is in, I am sure other things will come in, but I think there has been a strong consensus of the direction we need to go. Unfortunately, we do not make up the majority of Congress. We have got to deal with this on a basis of what in the national interest is the best energy policy for this country and what it does for us in terms of defense. It must provide long range consumer assurances that there will be adequate supplies of petroleum and energy found in this country at a reasonable price.

We cannot sell an energy policy on the basis of the economic problems in Odessa, TX or west Texas, or the Permian Basin, or the chairman's area of the State. That is not going to sell to people in the northeast, who I think, very honestly, do not have a great soft spot in their heart for we in Texas who may be having a little bit of a problem. We have to, I think again, look at what we can develop and how we are going to have to sell this program. Any changes that potentially can be made, must come from very specific directions, that is something that does not happen a great deal.

You are listing almost verse for verse things that need to be done, and I think we do strongly agree with that. What, from the professional end of it, and other than the generalities, in terms of national defense and in terms of national energy policy, that will

be good for the country—how do you suggest that we go about trying to sell to a Member, I use the term sell very broadly, I do not mean it literally but to sell to a Member of Congress who has no earthly idea about the oil patch, the problems that we are having, about the effects but that he sees a constituency that is reaping great benefits. We are seeing it happen in the economy, we are seeing some of the best economic indicators. As you have indicated, things are getting better, is there someone else up there.

But we are seeing good signs in the economy nationwide and those people who are going to have to vote for a policy that their constituents could come back and say, gee, look here you voted for this and look what happened to our gas price, whatever. How do you best suggest that we do that? What advice could you give us in trying to cater to that Member of Congress whose support we have got to have?

Mr. ABEL. Mr. Congressman, I will respond to that. I think you could probably approach Tip O'Neill, and he understands the shoe industry, that most of the shoes made in the United States are up in the northeast and they are protected with a tariff on shoes coming from France or Italy and so forth. I think most of the young ladies tell you the shoes that they buy come from foreign countries and they are tariffed, there is an import fee on those. I think by explaining it along those lines that maybe you could get the point over.

Mr. COMBEST. I think some of the problems that we are having internationally in trade areas makes those of us who consider ourselves free traders, unless free is going to be fair, take a second look. I think we need to always be able to totally reassess the positions we have taken. Those factors will help certainly with the comparisons and parallels we can draw.

Mr. McCoy. I think that one of the biggest tasks for our industry today is educating the people in Washington on the oil industry. In my travels and with the people I talk to from the Northeast, I find their concepts of the oil industry are a lot different than the actual, and a lot of it is based on the media. I hate to say this, but the program Dallas on TV has given us a pretty bad name in this industry.

I suggest that would be the starting point—to educate the people. I first realized we had a problem when a Congressman from the Northeast came down to take a look at the industry and he admitted that he was somewhat displeased with the industry. He had bought an automobile that ran off of diesel because diesel prices were cheaper. We quit drilling diesel wells and the price of diesel went up. So he was a little concerned.

I knew that we needed to spend more time educating the people in the Northeast and the other Congressmen and Senators from nonproducing States. I know talking to you is like preaching to the choir, but I really do not think they understand the industry and I think that is basically the crux of our problem.

Mr. COMBEST. Unquestionably, and we can sell that. I guess one of the things that really came home to roost to me was when a nameless Member of Congress from a significant producing State, very heavy in production in his area, commented to me on the House Floor that after a fairly lengthy term—I am trying to be

very vague about this—in Congress that he is finally beginning to understand, as a result of the problems in the energy industry, some of the arguments those of us within agriculture in our districts, have had for so long. But not until it reached home and hit his people, his constituency, did he begin to look closely at it. In the past, and you can count it, you can look at the Congressional Record for the past several years and every time there is an agricultural bill, this particular Member of Congress voted against it.

The problem is it has got to reach home, and it has got to be something of significance to them. The stories were told years ago about our energy policy and what was going to happen, and it was great. People could stand up there and say we had energy shortages in this country and say, "See, I told you so," but that is not doing a whole lot for the industry. We can stand up some day if something does not happen, I hope we never have to do that and say, "See, we told you so." We have got to work now within that system to get our message across. We need your help because as Congressman Stenholm said earlier, we do not have a great deal of credibility when we start talking to someone about the livelihood of our constituency coming from the oil industry and we start talking about our problems. They immediately begin to connect a lot of that concern with how really interested we are in some other things. Evidently, it is happening because we do have a credibility problem.

Mr. BEVERIDGE. Congressman, it seems to me that you have a pretty strong opportunity right now to talk to your colleagues who are hard to convince. The world situation is being controlled by Sheik Yamani, oil minister of Saudi Arabia because they have the ability to, I believe, easily produce 10 million barrels a day. Over the past 18 months, Mr. Yamani has told the world that he is trying to—you gentlemen from Texas will understand—he is trying to create a world railroad commission. I think he has correctly recognized that there is a temporary world oversupply and he is trying to get some sort of a regulatory scheme going that would give us a worldwide stable price that the chairman was talking about earlier.

Today he is demonstrating his power. He can bring the price down and he can bring it up like he did in 1972. And in order to counter that, to the best of our ability as a Nation, we have got to develop and continue developing our reserves. During the last 15 years, only one year—1981, were we able to replace the reserves that we have used in this Nation and that is just not enough. The historical facts are there and the present example is there and we must recognize it. He is telling us but Congress just will not listen.

Mr. COMBEST. History is on our side.

Mr. BEVERIDGE. Well, yes; and it is a really clear example today and finally, Saudi Arabia does not like to sell their oil for \$5, \$10, or whatever, they want a high price and you cannot blame them. That is what Mr. Yamani is trying to achieve and it is going to happen. We are going to get a better price in this country and I personally think it will be soon but we do have an opportunity for Government to reduce their involvement in our business, and free us up because this involvement has built up over the last 15 or 18

years to the point that we were strangling long before—at \$28 a barrel this industry was hurting, hurting terribly.

Mr. COMBEST. One thing quickly Mr. Chairman if I may. I appreciate Mr. McCoy in your testimony the specific exploratory well figures for the period of January 1 through October 1985. I was in Washington in December of 1984 when the infamous tax bill was released. And continuous since that time we have talked about the decline based upon the uncertainty in the industry and if nothing else if this thing lives, and I hope, as Congressman Stenholm hopes, that it dies a slow and painful death, but actually at this point, I hope it dies fast. If we could do a date certain in that legislation, and nonbinding resolutions have passed both bodies of Congress asking a date certain, and knowing nothing would happen prior to a date, I think it would help to somewhat alleviate the burdens that that tax reform has imposed upon us by just that uncertainty out there. As long as that thing is looming and rearing its ugly head, unfortunately, I am afraid that is going to be a problem.

Mr. McCoy. I can add that they picked a good subject company from a small business standpoint. I had a small business when the tax reform puzzle came out and it got smaller.

Mr. COMBEST. Thank you, Mr. Chairman.

Mr. STENHOLM. Mr. Abel, you testified very strongly in favor of an import tax. Mr. Beveridge, I believe IPAA is at this point in time opposed to an import fee, am I not correct?

Mr. BEVERIDGE. Yes, sir; that is correct.

Mr. STENHOLM. Mr. McCoy, what is the position of the Permian Basin on the oil import fee?

Mr. McCoy. Well, I think we first came out in favor of the import fee but recently that has been rescinded and we are standing opposed to it.

Mr. STENHOLM. For the record, of the other two oil and gas associations that I have the privilege of representing, the West Texas Oil and Gas Association is strongly opposed to a fee, and the North Texas Oil and Gas Association is strongly in favor of the fee. So being the politician that I am, I have weighed the fact that I have constituents for it and constituents against it and in this issue I intend to go back to Washington and to represent my constituency on that issue.

There is certainly a division of opinion within the industry as to what exactly we ought to do and how we ought to do it. This creates some problems for those of us who have the privilege of representing you. There are valid points on either side, but I happen to be one to believe that an oil import fee makes extremely good sense. I endorsed it and cosponsored Jim Weaver's bill which is far from perfect in its current form, H.R. 1396. I cosponsored this bill on March 4, 1985, because I believed that Sheik Yamani was going to do what he has done. I believed that the Saudis, with the capability of controlling the market, would not be the patsies of the supply and demand scenario forever. I did not believe they would cut their production from 10 million barrels a day down to almost 2 and let the rest of the world produce all the oil that they wanted at the price that they were supporting it at.

West Texas tractor seat common sense told me that this was not going to go on forever, and it would have been good policy for us to

have had in place an oil import fee. I realize that putting one in today is a little more difficult than if we had had that in our national policy. I also borrow on some of my experience and expertise in the area of agriculture and recognize that in some instances we have import fees that are working very well, wool and mohair for example.

We have a tariff on the importation of wool and this has preserved some semblances of a domestic industry, and I suggest not to the detriment of any consumers. The question is whether you want a domestic industry or not, and I think we are faced with that in the oil and gas industry. Some of the decisions that we are going to make boil down to whether we are going to attempt to control our own destiny or whether we are going to be completely at the mercy of someone else to do it.

Mr. Abel, I particularly appreciated your recognition that there is no such thing as a free market. This outlook completely disregards the fact that the majority of oil and gas produced in the world today is produced by foreign governments. The only way to have a free market under those circumstances is if all governments participated. Our Government takes as a national energy policy the idea that we are going to somehow work within a free market; this causes difficulties.

Agriculture polls show today that there is stronger support in urban America for helping the farmer than there is in rural America. Do you have any indications that the same situation exists when we talk about problems within the oil patch? I was very disturbed with those national polls that showed that actually we now have stronger support for the plight of the farmer in urban America than we have got in rural America. I suspect that is true in the 17th district.

Do you have any indication that the same attitude exists within the oil patch? Are there enough people in Odessa, TX that understand that their job, their livelihood, their pay check is dependent upon this industry or is there a sentiment that the oil and gas industry is getting what it deserves right here at home?

Mr. ABEL. I think there is a possibility that that may exist in Midland, TX, and I use the example that recently application was made to drill within the city limits and by the time the hearing was over with, why the city council denied all of the permits but one.

Mr. STENHOLM. Mr. McCoy, Mr. Beveridge, do you have any comment on that?

Mr. BEVERIDGE. My only comment would be traveling in different towns in the State of Texas that people are more aware of the ripple effect down through our State economy because of the downturn of the oil industry than expressing sympathy for me, petroleum geologist or an oil producer and yet I do not see any antagonism if that is the word—like they have got it coming or something like that, I have not seen that. But I have seen more of an awareness of other industries that are being hurt by our downturn.

Mr. STENHOLM. Mr. McCoy.

Mr. McCoy. I think I would call it more complacency than antagonistic. I know a year ago the IPAA put on a program here requesting some executive directors to explain to Odessans the

impact the tax reform bill would have on our economy. We sent out invitations to all the members of the Chamber of Commerce and the faculty of the college, University of Texas Permian Basin as well as some individuals. The total number of people that showed up was the man who mailed the invitations from the Odessa Chamber of Commerce. So I do not think it was antagonistic, I think it is complacency.

That may not be true today because a lot of people who did not come are now unemployed or out of business.

Mr. STENHOLM. I think the term complacent is probably better than the term antagonistic, and I think this describes the situation in agriculture as well.

Mr. Combest and I both serve on the Agriculture Committee as our major committee assignment. My district has 35 counties and is an agricultural, oil and gas, small town, small business oriented district. Very often I am confronted by individuals who ask if I pay attention to anyone besides the farmers. My answer is very quick; you bet I do.

Ninety-two percent of my constituents in rural west Texas are not farmers. Even less are oil and gas producers in terms of percentage. I tend to lump these two industries together and I suggest that there is a lot more that we as west Texans can do to help than we have done in the past.

As we grapple for solutions, we have a selling job to do at home.

West Texans have a proud independence, and we just do not like to ask Washington to do anything because we are afraid we are going to get what we ask for and a little bit more.

I am so glad to see oil and gas testimony acknowledging that there is no such thing as a free market. That is a giant step in the right direction of beginning to consider solutions to address the problems.

I have one other question I would ask for the record. Would you spell out what is involved in plugging a well and the costs for plugging stripper wells? What are we talking about in terms of cost to an individual who is today producing from one of these wells and then actually going in there and plugging?

Mr. BEVERIDGE. Well, you plug the well in accordance with requirements of the Railroad Commission and depending on the usual circumstances, depth, location, a \$10,000 cost can be used as an estimate. It could be \$8,000, it could be \$15,000 but it is——

Mr. STENHOLM. A range of \$8,000 to \$15,000?

Mr. BEVERIDGE. Yes, it is——

Mr. STENHOLM. That is the actual cost of plugging a well?

Mr. BEVERIDGE. To the producer.

Mr. STENHOLM. Those would be the necessary costs to meet the requirements of the Texas Railroad Commission and the environmental requirements, which we all support?

Mr. BEVERIDGE. Yes, sir; and today, you hear people talk—in the past you could recover some of the casing as used equipment and today you hear of people just plugging the well, leaving the casing in the ground because the value is not there so we are talking about if our Nation is—if our industry is faced with say plugging 100,000 wells, a tremendous economic loss figure not to mention

the loss of production, just the economic cost of plugging the wells properly.

Mr. STENHOLM. We have come a long way in terms of addressing some of the problems that land owners have had with oil and gas producers in the past. As bankruptcies occur, many of these small business operators are not going to have the \$8,000-\$15,000 to plug that well. What happens then?

Mr. BEVERIDGE. Well the—as I understand it, maybe Mr. Abel can add to it but there is a bond requirement in the State of Texas for example and that bond will provide the necessary capital to plug the well.

Mr. ABEL. There is also a fund that the Rail Commission maintains that if the operator is bankrupt and so forth, the Railroad Commission can do the plugging and they use the money out of that fund that has been created by the legislature. The legislature created it some time ago and a certain amount of money has gone into it; one of the items that goes into it is the commission fines on an operator for a violation of some of their rules and regulations; that goes into the plugging fund. And Mr. Beveridge was talking about just plugging the wells. I would say that if you plugged out a whole lease and you wound up with a tank battery that you had to remove or go some place with it, an old rusty tank, and restore the environment and level off the tank battery site then I would say that the cost could mount as high as \$20,000 per well.

Mr. MCCOY. I would like to comment on one thing on a plugged well. It is marginal that the cost of the plugging is so severe that the price of oil will never reach a high to where it is economical to go in and reopen that well. And some of your constituents feel that, so we shut in a few wells, when times get better we will open them back up and that is not true in a case of—these reserves will be lost forever.

Mr. COMBEST. That point I am glad you made, too, because I wanted to follow that for the record to get that statement, thank you.

Mr. STENHOLM. Whenever I hear somebody say forever, or no way, I am always reminded of the father that tells his son that he will never own a motorcycle, and the kid will own one before the sun sets that day. If oil went to \$100 a barrel, I suspect that somebody would try to drill a plug out and try one or two of these wells.

Mr. ABEL. It depends upon how much it cost to go get it.

Mr. STENHOLM. I am asking you now, would there not be some circumstances whereby some of these wells would come back into production at a certain price?

Mr. MCCOY. You would have to put the economics on it but I think a critical investor would put his money somewhere else.

Mr. BEVERIDGE. I have heard people talk along those lines that oil will have to be \$60 a barrel before we will go back into some plugged wells. So I think depending on the geology and the engineering in a particular lease, they might go back in but—

Mr. STENHOLM. You are saying it would have to be at a much higher price level than we have seen at the peak of the boom?

Mr. BEVERIDGE. Yes, sir.

Mr. STENHOLM. OK.

Mr. BEVERIDGE. So I think Mr. McCoy, his statement is accurate. But your question is also a good one because at some future date we might be compelled to—we might be happy with \$50 oil, I do not know what is going to happen in 15 years.

Mr. STENHOLM. Thank you gentlemen for a very excellent testimony. We appreciate your taking the time to be with us today. Our final panel consists of Mr. John Parish, Mr. John Landgraf, and Mr. Steve Late. Filling in for the Honorable Jan Fisher will be Mr. Tom Pace.

Mr. Pace.

TESTIMONY OF TOM PACE, FISCAL SERVICES DIRECTOR, ECTOR COUNTY, TX

Mr. PACE. Yes, sir; I am Tom Pace, I am the Fiscal Services Director of Ector County. I am here in place of Judge Jan Fisher who is in court today.

It is an honor to appear before this subcommittee to present our views and concerns on the severe economic conditions in west Texas and more specifically Ector County.

To fully realize the impact of the current boom and bust on Ector County, one must first look at the level of services mandated by Texas law and then examine the resources available to provide these services.

In 1980, Ector County had 115,374 residents based on a U.S. census. This total grew to a peak in 1982 of approximately 142,000. The best estimate of the current population is 132,254 residents, an increase of 14.6 percent over 1980. The county must provide a service to these citizens in the following general areas: Judicial, elections, law enforcement, corrections, highways, health, and welfare. All of these responsibilities are affected directly by an increase in population.

On the other hand, as our economy declines, our population likewise decreases. However, the decline in population has not led to a decline in the cost of providing services to the remaining citizens of Ector County. This is primarily due to the increased requirements and cost of providing adequate law enforcement, a judicial system and health and welfare demands.

As the price of oil increased, the resources required to meet this higher demand on services are available. However, the converse is not true. As the price of oil decreases, there is not a corresponding decline in the need for vital mandatory county services. Consequently, when the price of oil decreases, adequate funding is not available to carry on necessary county services.

The highest assessed valuation within Ector County was in 1983 with a value of \$6.1 billion. Since that time, the valuation has declined each year to a low in 1985 of \$5.6 billion. The estimated valuation for 1986 is \$5 billion, a decrease of 11 percent. This decrease in conjunction with expected tax collection rates of 90 percent in contrast to tax collection rates of 95 to 97 percent in past years means a major shortfall in funding.

In a county which has taken positive management actions to reduce the cost of government over a 3-year period, a shortfall in

tax revenues of over \$2 million cannot be accommodated within our budget.

During this same recessionary period, Federal programs for local governments are being greatly reduced. This factor makes our funding problems much more significant. We fully support the actions to reduce the deficit. However, it is respectfully requested that due consideration be provided to the west Texas area as to the impact of Federal action on our already depressed economy and additional burdens which have recently been placed on local governments.

Mr. STENHOLM. Mr. Parish.

**TESTIMONY OF JOHN T. PARISH, CITY COUNCILMAN,
ANDREWS, TX**

Mr. PARISH. I am John T. Parish, certified public accountant, Andrews, TX, the comptroller of a small independent oil company, a city councilman there in Andrews, also a director of the Permian Basin & Petroleum Association. Gentlemen, I would like to address the status of the independent oil and gas explorer and producer, outline some problems to be addressed: Falling oil prices, proposed tax reform, windfall profits tax, and a regulation of the NGPA natural gas prices.

The survival goal to be covered: The preservation of the domestic energy industry through nonpunitive legislation, regulation, and taxation.

Let me begin by sharing with you an excerpt from an editorial that appeared in the Andrews County News on March 27, 1986, written by publisher James Roberts. I think you could summarize the feeling of a lot of west Texas. It is probably undiplomatic to bring it up but a short refresher course in history in the continuing saga of the oil crisis might be in order. During the late 1970's, oil prices soared because OPEC took control of the market after Nixon regulated oil prices. The rise in the price of crude was so sudden, so steep, that new meaning was given to an old word "windfall."

Oil producers, especially in Texas, Oklahoma, and Louisiana were depicted as heartless vultures with obscene profits. The Federal Government passed the windfall profits tax to take away some of those obscene profits. The tax was a northeastern delight and an oilman's dilemma. The tax managed to extract so much money from Texas that for the first time in history, Uncle Sam took more proportionately from Texas and gave less back than any State in the Union.

When prices soared, "windfall" was the key word in Congress. Now that prices have dropped just as suddenly and just as steep as once they went up, have you heard the word "windfall" mentioned by any Congressman? Yet the dramatic drop in the price of crude has created similar windfalls for several industries. Lower fuel costs has created sudden windfalls for utility companies, the airlines industry, the shipping and trucking industries, certain transportation companies, and others since fuel cost make up a large part of their cost. So where is the clamor for a windfall profits tax on these businesses, where is the charge of obscene profits, where

is the debate over this new windfall that should be taxed for the benefit of all Americans?

Do not hold your breath until a new kind of windfall profits tax is passed. The American oil industry has been the whipping boy of Congress, the Federal Government at large, and the target of the American consumer for the past 20 years and no relief is in sight. When it comes to oil, what is sauce for the goose is not necessarily good for the gander.

Since the Arabs cannot get North Sea production cut, it would appear that the price of crude is going to remain low for a long, long period of years, to summarize Mr. Roberts editorial of last week.

Members of this subcommittee, I submit to you that the very survival of the domestic energy industry is at stake over the remaining months of 1986. The Nation is without a sound, national energy policy. The goal of being as energy self-sufficient as possible with a healthy oil industry has been abandoned. Posted prices have fallen as much as 46 percent in the last 10 weeks. Massive cutbacks and expiration development budgets have taken place by both major and independent oil companies.

The independent oil company that I represent has canceled plans for seven of the eight wells that were planned to be drilled in 1986. Development and maintenance expenditures have been suspended for all but the most critical of lease repairs. Payroll concessions have been sought and obtained from employees. We will maintain a positive cash-flow in the face of this downturned market. However, many independents have not achieved the maintenance of a positive cash-flow by the above measures.

The result will be a reduction in domestic production and a certainty that domestic reserves will drop by the end of the year. Even if the oil prices had not dropped this quarter, the independent oil producer faced punitive tax proposals. The Independent Petroleum Association of America estimates that if the provisions of Rostenkowski House bill, H.R. 3838, were currently in force, during the first full year there would have been \$11 billion tax increase directly as a result of eliminating expensing of intangible drilling costs and percentage depletion.

This increase equals 44 percent of the \$25 billion spent for drilling in the United States in 1983. For a typical independent, H.R. 3838 proposal would cause such drastic changes in cash-flow that over a 5-year period, each \$1 of increased tax revenue would reduce expenditures for exploration drilling by \$3 or more. The end result would be a short drop in the number of wells drilled and making America once again dangerously reliant on imported energy sources. Possibly Congress has forgotten the gas lines of the 1970's and merely looks upon the investment with the independent operator as a loophole in the tax law that is abused by the affluent when in reality it is the age-old problem of our legislators' basic lack of knowledge and understanding relative to the oil and gas industry.

The components of this tax bill are not reform within a framework of revenue neutrality, but a diversion of capital away from the oil and gas exploration and production into other investment activities.

I submit that a sound, national policy on energy would embody self-sufficiency as a basic premise and would call for the following: First, repeal of the windfall profits tax; second, deregulate the industry—this would involve repeal of the Fuel Use Act, repeal of incremental pricing, deregulation of pre-NGPA natural pricing and provide for the nondiscriminatory carriage of gas; third, eliminate provisions of the Rostenkowski tax bill H.R. 3838, that detrimentally affect the oil and gas industry; fourth, provide flexibility to the FDIC, the Comptroller of the Currency, and the Federal Reserve Board in allowing the restructuring of oil and gas industry debt; fifth, reject any form of oil import tax—an import fee would be a reversal of free market policies; and, sixth, preservation of the domestic energy industry through nonpunitive legislation, regulation, and taxation.

Mr. STENHOLM. Next, Mr. Landgraf.

TESTIMONY OF JOHN F. LANDGRAF, LANDGRAF, CRUTCHER & ASSOCIATES, INC., ODESSA, TX

Mr. LANDGRAF. Mr. Chairman, thank you for the privilege of appearing at this hearing today before this subcommittee. My name is John F. Landgraf. I live in Odessa, TX. I am a principal in the consulting engineering firm of Landgraf, Crutcher & Associates. However, I come to you today as president of the Greater Odessa Chamber of Commerce. When I took office in October 1985, west Texas intermediate crude prices were at \$28.35 a barrel. New spot market prices now are less than \$15 a barrel and I am sure as you have heard futures this morning opened at less than \$10 a barrel.

It has been suggested by many community members and some of my colleagues that someone else fill my unexpired term until we get this oil and gas business straightened out. As chamber of commerce president, I try to always point up and accentuate the positive aspects of the community but, for this hearing, I am compelled to give you the hard facts that are not very pleasant which have come about since my taking office. This is best illustrated by giving you the economic indicators that our chamber of commerce maintains on a routine basis. Rig count for the Permian Basin: March 24, 1985, total rig count was 317; March 24, 1986, the number of working rigs had dropped to 172, or a 46-percent decrease. Total employment and initial unemployment claims, in January 1985, there were 61,325 people employed here. By January 1986, that number had dropped to 56,000 and by February, the number of people unemployed was 54,000.

As expected, the initial unemployment claims have tracked this decline of employment. January 1985, we saw 540 initial claims made. January 1986 had 985 and the alarming news for February 1986 showed 1,543 new claims made. For the first 2 weeks of March 1986, a total of 954 initial unemployment claims were filed. According to the Texas Employment Commission's local office, the total for March 1986 is expected to reach 1,800 by this month's end or an average of over 95 new claims a day.

School enrollment: To further document the effects of the economic downturn, our public school enrollment from September 1984 to March 1985 showed an outmigration of 289 students. For

the same reporting period, 1985-86, we had 530 students leave our area.

New construction: New building permits have basically been flat with no growth within the last year. The only bright spot in that to distort those figures somewhat is a new U.S. postal facility and a new retirement center and both of these projects have been in the planning stages for several years and building permits were just recently issued.

- Office building and apartment occupancy: Office building occupancy has eroded from a January 1985 rate of 66.5 percent to a January 1986 rate of 63 percent and the lease rate per square foot has declined by a like amount of \$10.69 to \$10.36 a square foot. The recent figures are not yet in but should show below \$10 per square foot average based on rates from some of the larger buildings recent activities and discounting programs.

Residential apartment occupancy levels have fallen from January 1985, 90 percent, to January 1986, 87 percent, with lower rates expected as the current data is compiled.

Airline boardings have shown a decline as well just in the last month. January 1986 had 44,862 passengers while February 1986 had 42,900 passengers for a 4.4-percent decrease over that 1 month. This figure for February 1985 was 43,310 also showing a year-to-date reduction in passenger boardings.

I have attached these and other pertinent figures in tabular form for your use and study. There are many efforts for economic diversification underway by the chamber of commerce and area businesses. Some of these efforts have immediate impact while others are long range and will take years to accomplish. Should you desire information on these efforts, I will be happy to discuss them with you. Thank you very much for this opportunity to appear before you.

[Figures referred to above follow:]

SELECTED ECONOMIC INDICATORS

ODESSA, TEXAS

RIG COUNT	3-23-86	3-16-86	Zchange	3-24-85	Zchange		
Permian Basin	172	186	-7.5	317	-45.7		
EMPLOYMENT	2/86	1/86	Zchange	2/85	Zchange	1/85	Zchange
Total Employment	56,400	56,000	-2.9	61,723	-11.9	61,325	-11.3
Initial Unemployment Claims	1,543	985	+56.6	420	+267.4	540	+185.7

*For the first two weeks of March '86, a total of 954 initial unemployment claims were filed. According to TEC, the total for March '86 is expected to reach 1,800 by month's end, averaging 95.4 claims per day.

APARTMENT OCCUPANCY	1/86	7/85	Zchange	1/85	Zchange
City Occupancy Rate	87%	89.5%		90%	
# Units Occupied	7,908	8,142	-2.9	8,060	-1.9

OFFICE BUILDING OCCUP.	1/86	7/85	Zchange	1/85	Zchange
City Occupancy Rate	63.1%	66.8%		66.5%	
Available Square Feet	394,581	349,272	+13.0	355,452	+11.0
Average Annual Lease Rate	\$10.36	\$10.81	-4.2	\$10.69	-3.1

CONSTRUCTION	2/86	2/85	Zchange	2/84	Zchange
(Year to date)(000)					
New Residential	\$1,093.2	\$1,811.6	-39.4	\$1,670.0	-34.2
New Commercial	\$3,103.5	\$2,690.2	+15.4	\$1,950.0	+59.2
Total Construction	\$15,877.9	\$5,445.0	+191.6	\$4,609.4	+244.5

AIRLINE BOARDINGS	2/86	1/86	Zchange	2/85	Zchange
Total Boardings	42,900	44,862	-4.4	43,315	-1.0

ELECTRIC HOOKUPS	2/86	1/86	Zchange	2/85	Zchange
Total Hookups	56,109	56,156	-0.1	56,276	-0.3
Residential Hookups	47,250	47,326	-0.2	47,457	-0.4

CITY SALES TAX RECEIPTS	1986	1985	Zchange	1984	Zchange
Payments to Date thru period ending 2/28	\$2,051,890	\$2,105,750	-2.6	\$1,937,513	+5.9

SCHOOL ENROLLMENT	'85/'86	'86/'85
September	26,325	25,623
October	26,535	25,656
November	26,423	25,642
December	26,367	25,610
January	26,235	25,572
February	26,122	25,538
March	26,095	25,435
Sept./March Student Total	26,300	25,694

Mr. STENHOLM. Thank you. Mr. Late.

**TESTIMONY OF STEVE LATE, TEXAS AUTOMOBILE DEALERS
ASSOCIATION, ODESSA, TX**

Mr. LATE. Thank you, Mr. Chairman. My name is Steve Late from Odessa, TX, where I own and operate with my father a Chevrolet dealership here in Odessa. I am on the board of directors of the Texas Automobile Dealers Association and a current member of the executive committee of that organization. I would like to direct my thoughts today not only about the distressed state of the oil and gas industry but to also inform your committee of the domino effect that this industry has on the thousands of small businesses that are the heart of the American dream.

I would like to address my comments regarding the entire State of Texas. Because of my association with TADA, it keeps me very accessible to getting information regarding the automobile business. The first item that I would like to share with you concerns the month of February's comparison of the new-car sales in Texas' three major markets. While it may come as no surprise to you that current truck sales here in Ector County and Midland County are down in some cases up to 40 percent, I think it is most startling the sales results in Dallas County, Bear County, and Harris County.

In Dallas County, which is perhaps our State's most vibrant economy, new car sales in February 1986 versus February 1985 are down 14½ percent. In Bear County, which is primarily San Antonio, new car sales are off 7.7 percent. San Antonio, as you know, of course, is high technology image. The popular Mayor Cisneros is also beginning to feel the effects of a battered oil and gas industry.

But probably the most devastating market in Texas, because of its sheer size, is Harris County in Houston. While their sales were down almost 20 percent of the February comparison, that percentage equates to almost 3,000 car sales down from the previous period which equates to \$50 million worth of moneys not spent with the automobile dealers and their related suppliers in that 1 month.

Let me tell you some more about Houston. In oilfield machinery manufacturing which translates locally as the oil tool business, there were 51,700 employed in the peak period of March 1982, 20,900 in January of this year, the most recent month for which these figures are available.

In the field services category covering workers employed by companies that, for example, maintain drilling mud, there were 54,500 people employed in March 1982, 37,800 in January 1986. In the crude petroleum and natural gas extraction category covering those directly involved in drilling, there were 60,400 jobs in the peak period of June 1982, 51,500 jobs in January 1986. Now these figures were from the U.S. Department of Labor's Bureau of Labor Statistics.

From the month of March 1982 to December 1983, Houston lost over 150,000 jobs in the oil- and gas-related category. While they picked up 70,000 jobs in other industries, they are facing another possible loss of 100,000 jobs in Houston this year attributed directly to the oil and gas industry. On a recent visit to Houston, I came

across an article in the Houston Chronicle that really draws a picture of just how significant the downturn of this industry really is and I quote the Houston Chronicle on this: "But to get this area's economic base firm enough to regain the employment levels of 1981, 1982 would require a remarkable feat without a recovery in energy related business." And here is the key quote: "The city would have to attract 10 new Saturn plants, 10 new Navy ports, 10 computer firms, a completely new medical center solely devoted to out of town patients and a second space center at least as big as the Johnson Space Center." That really kind of brings it home to me.

Although March sales—this is car sales I am talking about here—reports are not finished yet, I did a random telephone blitz to some various car dealers across the State and evidently February is only the tip of the iceberg. My phone conversations consisted of lengthy conversations about how many people each dealer has or already had laid off and we have done that here in Odessa and Midland.

I think the unemployment figures most recently announced in Texas are going to hit 12 percent statewide by the end of May. According to the Railroad Commission, Texas oil production is down 32 percent and gas production is down 39 percent in Texas in a 12-year period from 1972 to 1984. There are only 443 rigs working now in the State which is the lowest State rig count since 1974. And here in the Permian Basin in 1982, there were over 500 rigs active, there are now less than 170 rigs working in the basin.

The last few minutes I have shared with you some information about the automobile business in different Texas markets. I have shared with you a picture of a devastated Houston and the effects the downturn of the oil and gas industry has had on that city. But the real victims that this industry downturn affects are the 16 million people that live in our great State of Texas and the several other million people that live in the States highly concentrated with this same industry, Oklahoma, Louisiana, New Mexico, to name a few.

I am talking about real America, the appliance store owners, the gas station attendants, restaurant personnel, all these, they are small, family businesses that make up the heart of America. I am talking about the people that make their communities prosper, their chambers of commerce, their schools, their civic organizations. It all suffers and is suffering today right here in Odessa. I think the average Texan would tell you that he'd just as soon the Government not meddle in his business but they have meddled in his business with the windfall profits tax, and the regulation on prices of natural gas, and they did meddle with Chrysler to keep it afloat, and they did meddle with the auto industry on the Japanese cars by imposing an import tax or restriction at a 75-percent import tax on Japanese trucks, and they are still meddling with the agricultural business with all their subsidies which we hear more today is probably deathly necessary.

But I do not recall Congress asking Chrysler for a windfall profits tax on its recordsetting profits the last 2 years. So, since Congress is going to meddle then let's either set some policy to help this ailing industry while it is down or set some policy to not tax

this industry so heavily when it is up. Incidentally, if one marks the current downturn in the oil industry, the last domestic downturn lasted approximately 1961 to 1975, or a period of 14 years, it would not be unreasonable to assume that the domestic U.S. industry without a major change in the world supply due to conflict in the Middle East or some other external force not within the control of the U.S. industry it could last an additional 8 years if it compares with the last time.

Ladies and gentlemen, Texans cannot survive another 8 years of this nor can our neighbors on all sides. I ask your committee to truly consider the many effects that your legislation has on American small businesses that operate in this region of the country and I ask you to be fair and consistent with your policies to help this oil industry in both the good times and the bad. Thank you.

Mr. STENHOLM. Thank you, Mr. Late. Mr. Combest.

Mr. COMBEST. Mr. Landgraf, I am glad to know that it is you that the people are blaming for the problems in the industry, it gives me a great deal of relief.

Mr. LANDGRAF. Just on the local level.

Mr. COMBEST. Can you, based on a combination of figures that were available to the chamber to individual businessmen to the city, or county, or whatever, give me an estimate in percentages of the number of families in Ector County whose primary income source is from energy-related types of businesses or employment?

Mr. LANDGRAF. We have been asked that question and we do not have that broken out specifically because I think as always testimony showed everybody is affected.

Mr. COMBEST. I guess what I was trying to get to Mr. Landgraf is if there had ever been where directly a paycheck is by support or supply industry. I would suspect Steve Late anticipates his income is directly related to the oil and gas industry or the energy industry in this area. There were some statistics in here but what was the—do you have the figures on the migration or movement out of the county since the first of the year?

Mr. LANDGRAF. I have just the thing that we tried for the school enrollments for school-age children and since—we have had 530 so far in just the school-age children that have left the community.

Mr. COMBEST. And that has been this calendar year so far?

Mr. LANDGRAF. Yes, sir; that is for September school year until the end of March.

Mr. COMBEST. And in the March period of time the unemployment was up over 1,000; 1,003 I believe from—

Mr. LANDGRAF. From initial claims and in this month initial claims are expected to be around 1,800 and then the first 2 weeks we had for that 954.

Mr. COMBEST. A good point, Mr. Pace, in Judge Fisher's testimony was that there is not a decline in the cost of service that directly proportionally relates to the decline in county income from your tax base or even from a movement, a movement of people out of a county. You still got a level of cost incurred there and law enforcement in all the other areas that you mentioned that remains fairly constant. Has there been any projections done and participations of what the shortfall, based on current tax this year, would be, what your shortfall would run in accounting for the annual?

Mr. PACE. Just on the taxes, Congressman, it is going to be in excess of \$2 million. When we take that in combination with other actions, Federal revenue sharing zeroed out in excess of \$800,000. Gramm-Rudman having an impact on the Nutrition Program for the elderly. Anyway, the Nutrition Program for persons over 60 years of age, I will put it that way is being reduced. In other things, we are going to have a significant shortfall.

Mr. COMBEST. You are talking a total of \$2 million just in tax base revenue?

Mr. PACE. Just in tax which is directly related to the price of the petroleum.

Mr. COMBEST. Chairman Stenholm pointed out in the beginning of his testimony, beginning of the hearing today, it is significant that because we do not write the energy legislation in the Small Business Subcommittee, we do not write tax legislation, hopefully we can because of our interest and concern have something to do with the writing of that that I think the testimony that we have gathered here today is excellent, all of your testimony and statements were great and I think there are a couple we can use to further the concern.

What we can I think also project is to me what is the real heart of the issue of the way that on a very parochial basis if I may that it concerns me and that is how it affects the small business operator, whether he is an automobile dealer, whether he is a TV salesman, whether he has an appliance store, whether they have a flower shop, whatever it may be, but normally in peoples minds are totally unrelated to the energy industry because they do not get their check from X major independent or X major oil companies. Those are the ones that we are really getting into—that are really being affected, all of their businesses, the domino effect, the problems in banking are going to continue to be difficult on them as well because the projected incomes are obviously going to be down and their sales are going to be down. Having come from a small business that I founded in 1978 prior to my current occupation, I was very well aware of this and we could see exactly how that flow moved up and down in the sales of electronics but it had nothing to do with the oil and gas industry directly but you can appreciate that.

Our whole area with the effect of agriculture and energy right now is probably one of the most significant hits that we have taken in our region I think, and probably in Congressman Stenholm's district and mine, in many years. It is far reaching and it is concerning. It is something I think that we have got to deal with. The interesting thing is that you are saying here as nonproducers what it is that the industry itself is saying that needs to be done. You are talking oil, and gas, and energy today and how those effects are going to have something to do with you.

Mr. Landgraf, I can appreciate where you are coming from in this. We all I guess face those concerns and problems from time to time. Hopefully there is something that we can do, hopefully there is something that can change and can make a significant difference. Mr. Parish, I noticed that in your testimony you were opposing the oil and import fee which again Congressman Stenholm pointed out earlier is the industry itself is not even set on and

there are some very adverse opinions about that, whether or not that loan is the answer.

But I think the basic direction is the same, what I hope we can do is continue to work together on the thing. I would be very interested in particular what comes from the chamber and what comes from the county as your figures change, as those figures are consistent, I would like, on a personal basis, and we could certainly submit it to the committee for at least their consideration, I would like to be continually updated on those figures to really get the significance of what it is.

Mr. LANDGRAF. I think a lot of those things—some of these were yearend figures, I believe a lot of them are going to change unfortunately dramatically just in the events that have occurred in the last 3 months so we will be happy to update you.

Mr. COMBEST. Gentlemen, thank you very much, Mr. Chairman.

Mr. STENHOLM. Mr. Late, it was very interesting testimony that you gave in light of the implications of the decline of the oil industry and what is happening in the car market in Houston, Dallas, and San Antonio. Do you have the figures for the rest of the Nation for a comparable period? Regarding the decline of auto sales in Texas, has there been an increase in the other areas of the country?

Mr. LATE. No; there has not been an increase, it has been flush. I am talking about domestic industry more or less now and when you start throwing imports in, your national figures are still on a level basis from February to February, there were some national sales contests going and stuff that they have to take out to compare with. These figures are significant because they are considerably less than national prices. I was sitting here thinking awhile ago when I heard you make a comment to the other panel on the effectiveness and lack of sympathy from other congressional people on this issue. And I think this thing is going—you might be coming to have a couple of allies more than you think here in the next 60 to 90 days. What I mean is, for instance, General Motors right now is sitting on 100 days, over 100 days, 110-day supply of vehicles, cars, and trucks. It is the highest inventory they have had in the history of GM.

Now the significant thing about that is right here you see 25 percent of truck sales in the United States or in the State of Texas, when you take Texas, Louisiana, actually what we call the Dallas region, this Chevrolet division of General Motors of the Dallas region consisted of Dallas, Houston, San Antonio, Oklahoma City, and New Orleans, and New Mexico, part of New Mexico. If you add those together, you are talking about over a third, almost 40 percent of the truck sales in the United States that is with Ford, and Dodge, and all added together in imports.

So, when the sales begin to come off as dramatically as they are, they are talking about effects, a huge decrease in their sales on 30, 40 percent of their sales. So, you may begin to have some allies but this domino effect, this oil and gas energy is not just affecting Texas, New Mexico, it is going to affect the consumer everywhere when their sales begin to fall off because they are going to have to—the Arlington plant is shutting down this month. The Camaro plant in Van Nuys, CA, is getting ready to shut down. Of course,

there are plants all over the ranch so I think that some of these things you may begin to see some allies because the oil and gas industry is just huge and when the buying effects, when Arco, and Amoco, and Exxon cut their exploration budget 70 percent in the United States in some cases, you are talking about trucks and cars that are not being bought and, therefore, if they are not being manufactured, and not being sold, people are going to be laid off because they are not selling. So you may be getting some help here in another 2 or 3 months that you might not be expecting by some allies here.

And I am just talking off the top of my head but I do see that as a very real possibility.

Mr. STENHOLM. I was very interested in your comments regarding the overall condition within the automobile industry and its effect on the economy. I think you are right on target. You are giving some credibility to the study by the Joint Economic Committee which Senator Lloyd Bentsen requested. Briefly, this report concluded that the extravagant claims for a dramatic resurgence of economic growth due to falling oil prices are without justification. Real GNP this year will rise less than 1 percentage point due to lower oil and energy prices, and nearly 80 percent of the impact of falling energy prices will be offset by eroding revenues to the domestic energy sector and resulting ripple effects.

One thing this subcommittee is going to look into very carefully is the small business perspective of the drop in oil prices and the impact within the U.S. energy industry. We hope to be able to contribute to the type of national energy policy which the witnesses have advocated today.

We have differences of opinion as to whether we need an import fee or whether we do not, and what needs to be done. Mr. Landgraf, I would suggest as president of the chamber of commerce you might try blaming the board of the chamber for the current problems.

Mr. LATE. Wait a minute, you are talking to me, too.

Mr. STENHOLM. I am just talking about self-preservation. I am just trying to be helpful to you. I do not have any other particular questions. I think your testimony, particularly this last panel, certainly underlines in red ink the problems of Odessa, TX, this region, and how you are having to deal with them at the local government level as well as from the personal and private enterprise levels. The gentleman to my right is Mr. John Haugen; he heads up the Small Business Subcommittee staff. He is the staffer who will take this hearing record and will begin to put it together, working with Mr. Combest's staff. Mr. Combest, on behalf of myself and my staff, we thank you and your staff for the cooperation you have provided in setting up this hearing, securing witnesses, and helping with all the other logistical arrangements such a hearing requires.

Thank you for inviting us to Odessa. We are happy to be here and we look forward to welcoming you to Abilene tomorrow. We will reconvene tomorrow at 11 in Abilene. Do you have any final remarks, Mr. Combest?

Mr. COMBEST. Mr. Chairman, I appreciate the fact that you would come out here. I think you can tell from the testimony the

concern that people have is real. We appreciate your interest, concern, your knowledge of the problems that confront west Texas, and that we have adjoining districts, and we have so many similarities. You are a capable leader in the House of Representatives. It is a pleasure to work with you, with your staff.

Jenny Welch of my Odessa office, we appreciate very much her help, and the city of Odessa for the use of the chambers here for this hearing, and the interested people who have come. These sometimes get long. I appreciate your patience and your concern, we are interested. We look forward to working with you and hopefully this will be productive. Again, Mr. Chairman, you honored us by coming to Odessa and you are welcome here anytime.

Mr. STENHOLM. Thank you. Is there anyone in the audience that might have a statement or a solution they would like to make at this time? We would take just a moment to hear from you if you so desire to be heard.

Mr. SPANNUS. Mr. Chairman, I think when you made the comment about the west end of Texas——

Mr. STENHOLM. If you would identify yourself, please.

Mr. SPANNUS. Excuse me, I am Harry Spannus, executive vice president of the Permian Basin Petroleum Association. I think west central Texas' position on oil imports was against crude oil imports but there are four refined products imported; is that correct?

Mr. STENHOLM. Yes; that is the way we understand it. We thank each and every witness today for their excellent testimony. We hope it will be helpful to the resolution of some of the problems. Thank you for coming. This hearing stands adjourned.

[Whereupon, at 12:03 p.m., the subcommittee adjourned, to reconvene subject to call of the Chair.]



FUTURE OF INDEPENDENT OIL AND GAS EXPLORERS/PRODUCERS: MARKET TRENDS AND TAX REFORM

WEDNESDAY, APRIL 2, 1986

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON ENERGY, ENVIRONMENT, AND
SAFETY ISSUES AFFECTING SMALL BUSINESS,
COMMITTEE ON SMALL BUSINESS,
Abilene, TX.

The subcommittee met, pursuant to notice, at 11 a.m., in the Royal Inn, Highway 80 West, Abilene, TX, Hon. Charles W. Stenholm (chairman of the subcommittee) presiding.

OPENING STATEMENT OF CHAIRMAN STENHOLM

Mr. STENHOLM. Good morning. We welcome you to this hearing and meeting of the Subcommittee on Energy, Environment, and Safety Issues Affecting Small Business. The meeting will now come to order.

This is the second day of hearings on this topic for the subcommittee, which I have the privilege of chairing.

The subject this morning is the future of independent oil and gas explorers/producers: market trends and tax reform. An identical hearing was held yesterday in Odessa.

Joining me is my friend and colleague, the Honorable Larry Combest, who represents our neighboring district to the west, the 19th District of Texas. In addition to our west Texas heritage, Larry and I both serve on the House Agriculture Committee and the Small Business Committee, as well as this particular subcommittee.

I would like to extend a warm welcome to the witnesses that will appear before us today, and to others who are in attendance here today. It is particularly good to see this crowd showing the interest that I know we all have in the subject before us.

Let me also take this opportunity to express the subcommittee's appreciation to the Royal Inn, particularly to Ms. Mit Barfield, for making this facility available to us today.

It is no secret that U.S. oil and gas explorers, producers, independent producers, majors, et cetera, are suffering from a severe depression, the effects of which are immediately devastating to the State of Texas and potentially catastrophic for the Nation's economic and national security.

Independent producers, who historically drill some 86 percent of the developmental wells and 90 percent of the wildcat wells, have

all but abandoned the search for oil in the United States. If this situation continues, U.S. proven reserves will shrink as we fail to replace our reserves with new discoveries.

The United States currently imports one-third of its crude oil supply and depends upon its domestic oil and gas industry for the remaining two-thirds. Coupling the projected production decline with the expected increase in imports, imports may soon total 53 percent, and we have heard some predictions as high as 60 to 65 percent. Based on our experience of the 1970's, this scenario is cause for deep alarm for everyone concerned with our national security. It is a risk to our economy and the long-term well-being of our consumers. The negative impact of low oil prices on U.S. crude oil production will have a greatly accelerated effect as the perception of permanence sets in.

The price slide of the past 90 days is not the result of supply and demand market economics. It results from punitive, monopolistic actions designed to undercut high-cost producers by the world's single most dominant producer. Saudi Arabia has embarked on a course to recapture what it perceives to be its share of the world market. Over the past 6 years, the Saudis have seen their share of free world production decline from 19 percent to 6 percent.

At this time, I believe there are legitimate reasons to justify the creation of a fee on oil imports, apart from the need for additional revenues to reduce the massive budget deficits. The United States cannot avoid an increasing reliance on undependable petroleum imports unless major steps are taken to increase domestic exploration and development of oil and gas, and to extend the lives of marginal oil and gas properties.

The drive within Congress to enact tax reform legislation remains alive. I opposed the House version of such legislation because of the punitive energy tax provisions contained in the House bill, H.R. 3838. The initial Senate effort, as introduced by the chairman of the Finance Committee, would retain present law for domestic production of oil and gas. These circumstances leave the door open for a possible House/Senate compromise giving us something between the House bill and existing treatment of intangible drilling costs and percentage depletion.

The problems within the domestic oil and gas industry are many and varied. This subcommittee wants to build a hearing record to take back to Washington for consideration and reference as the Congress and the administration prepare and implement policy to address the current, as well as the future, energy situation.

Last year, our subcommittee held hearings regarding the small business impact resulting from the moratoria on offshore oil and gas exploration. We were concerned at that time about the effects the moratoria were having on small businesses, particularly in California. We would like to believe and would like to take a small amount of credit for the fact that the moratoria were lifted as a result of some of the hearing evidence that we gathered. I was very surprised at the impact on small businesses throughout the Nation as a result of the slowdown in offshore oil and gas exploration and development. We find in so many business endeavors that there are often small business considerations that get overlooked during the heat of debate in the Congress.

One of the problems we have today in dealing with the current economic crisis within the oil industry is that there is very little sympathy anywhere else in the country. Our colleagues and their constituents still remember the bumper stickers in Texas a few years ago that said "Drive 70 and Freeze a Yankee." It was funny then; it is not so funny today. And it shows some of the short-sightedness that we all have at different periods of time, whether we were participating in the last boom or the current bust. I happen to be one of those who believe that no one benefits from boom and bust in the energy business or in the agriculture business. Price stability is extremely important to the modern world of energy economics.

Therefore, we hope to glean some information today, as we did yesterday, in looking for some potential solutions. I would point out that the subcommittee has no primary jurisdiction. Taxes fall under the jurisdiction of the House Ways and Means Committee. Regulatory policies go before the House Energy and Commerce Committee. What we do have is oversight jurisdiction over energy, environment, and safety issues affecting small business. We hope to take this testimony, build a record, and utilize it in testifying before the appropriate committees. We also hope to have input into the legislation which will address the current energy crisis. Hopefully, we will be able to contribute information which will be useful to the formation of a national energy policy which our Nation so desperately needs. You can rest assured that we will be educating our colleagues as to just what is happening in the oil patch.

With those remarks, I would now like to recognize and welcome my colleague from Lubbock, TX, Larry Combest, serving his first term for the 19th District. As I mentioned earlier, we have the privilege of serving together on the Agriculture Committee and the Small Business Committee.

Larry, I welcome you to the 17th District and Abilene, TX, and I recognize you for any remarks that you might care to make at this time.

OPENING STATEMENT OF HON. LARRY COMBEST, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. COMBEST. Mr. Chairman, I appreciate it. I want to first of all commend you for hosting this hearing. I certainly think it shows a tremendous amount of foresight on your part to have a hearing in such a speedy fashion, realizing the problems we face are not only in the west Texas area, but certainly statewide.

We had an interesting hearing yesterday in Odessa. I suppose someone summed it up very well at the end of the hearing by saying that we really did not hear a lot of good news today. We really did not go there to hear the good news. We went there to be able to put some comments and concerns in the official record that people expressed about things that were happening to them. Some concerns were directly related to the oil and gas industry from the production standpoint. Some were related to problems in terms of supply and support-type industries. And some of the witnesses owned businesses totally unrelated to the oil and gas industry. Their income did not come directly from it, but obviously they realized

the impact on their income and the drop in that caused by the problems that were being experienced and they were facing in the Permian Basin.

As Chairman Stenholm mentioned, there were many of us, particularly from the producing States, who strongly oppose the House-passed version of the tax reform legislation for a number of reasons. We could spend a day discussing that; particularly—and one of the main reasons for our opposition was the treatment of the oil and gas industry.

It is something that is critical. I think you will find that in this situation you will basically—if I can use the phrase—be preaching to the choir, because we are familiar with, we are understanding of, and we are sympathetic to, the problems that are being experienced not only, of course, in the energy industry but in agriculture as well.

Congressman Stenholm mentioned the fact that we do serve together on two committees. I will tell you as a freshman Member that we look to his leadership because of his reputation and the respect Charlie Stenholm has in the Congress.

We do hope to gather further information today so we can use it to help in persuading and selling—if I may use the term—our colleagues as to the problems that we are experiencing. The Congressman certainly summed up the problem when he said we cannot sell this in Washington on the idea of, we're having economic problems in west Texas. Some people really do not care. They do recall the bumper stickers; they do recall the attitudes. So we cannot go up there and say, I'm having a difficult time in Odessa, TX economically. Charlie cannot say he is having a difficult time in Abilene and the rest of his district. We have to look at this on the broad scale. We have to look at it in terms of developing a national energy policy. The condition of the oil and gas industry affects the national defense of this country, and everyone has got to recognize that it is in the long-range best interest, both from a security standpoint and certainly from an economic standpoint, that we are self-sufficient in energy in this country.

With that, I will yield back my time. We look forward to having your testimony. And, again, I compliment Congressman Stenholm as chairman of this subcommittee for holding these hearings.

Mr. STENHOLM. We will call the first panel.

Mr. Manuel Mullins and Mr. Buddy Baldridge, if you will take your places at the table, we will hear from you first.

We have four panels. I would ask each of you to summarize your prepared statements. The complete text of your statement will be made a part of the official record, along with your spoken comments.

While you are getting ready, I will read part of one letter I just received indicating a misunderstanding with regard to these hearings:

Dear Representative Stenholm: Talking about the hearings you are about to hold in Odessa and Abilene, I commend you for it. But if I may, I would like to make one suggestion; that you extend your hearing to cover all field service contractors and suppliers.

We thought we made it very clear that we were, in fact, making this forum available to everyone. We hope to hear from small busi-

nesses affected by the current energy situation just as we hear from those within the oil and gas business. We need to know how everyone is being affected.

So we hope that if there was any misunderstanding, that it has now been cleared up. If we have time prior to our adjournment at 2 p.m., we will take additional witnesses or statements or questions from the floor.

With those comments, I will welcome, first, Mr. Manuel Mullins of the M.W. Mullins Oil Co., Olney, TX.

Manuel, welcome.

Mr. MULLINS. Thank you, Charles and Larry. I am proud to be here.

TESTIMONY OF MANUEL MULLINS, M.W. MULLINS OIL CO., OLNEY, TX

Mr. MULLINS. Charles, I was proud to be asked to be here today and give my views on the future of the independent oil operators.

I own and operate several shallow oil leases in a 12-mile radius around Olney, TX. My business is a family-run business. My son-in-law assists me in the day-to-day work on the leases, and my daughter keeps the books and makes all the records. We have an office with a shop in the back, 1 mile east of Olney. And my son-in-law and I constructed it. We constructed our own well service machine and a shop, and do all of the work, maintain, and operate these leases.

The total wells that we operate are 25, with an average production of a barrel-and-a-half per day per well. The accumulation of these wells, for me, represents a lifetime of work, but the future and the short term looks pretty bleak. Most of these wells are old pools that were plugged out in the 1950's and were redrilled in the 1970's. If the price of oil remains below \$20 a barrel, most of these wells will be plugged in the next year or two. This is all settled production and it would mean 14,400 barrels of oil per year would be lost because it would be economically impossible to redrill these wells.

We work long hours, 7 days a week to keep these wells going, and are happy to do so if we can operate at a profit, and a meager profit at that. We are burdened by a continual rise in electric bills. My rural electric co-op bill went up this month alone 7 percent over the previous month's bill on the same amount of kilowatts.

I am going to add to this that our fuel adjustment went down this month. We actually had a minus fuel adjustment bill, but our regular bill went up 25 percent. By the time the fuel adjustment came off of it, it just amounted to 7 percent. So if the energy had not gone down, we would have had a 25-percent raise in our electric bill in 1 month alone. But by the time it averaged out, it was just 7 percent.

The things that we have no control over is what is killing us. The things that we need are: We need a minimum price of \$18 to \$20 a barrel to break even. And this means no new exploration or drilling to maintain the current production. And, No. 2, if we are to stay in business, we need lower utility bills now. If so, we have a chance to stay until the price goes up. If the price does go up, we

will need depletion and then intangible drilling costs left as they are, if there is going to be any new drilling to speak of.

It might not be important to anyone but my family and me that I am able to stay in business and produce these wells. But it is very important to the country as a whole that these wells, and wells just like them all across the oil-producing States be kept producing.

In 1968, the oil producer in Texas was producing at 45 percent of allowable. In 1970, he was producing at 87 percent of allowable. And in April 1972, the State starting producing 100 percent of allowable, and with the exception of 3 months, they have been doing so ever since. The country cannot afford to go through what it did in the 1970's because of the shortage of oil. The country and the producer in some way need to figure out a way to keep these wells producing and the oil business healthy.

As far as a solution, I do not really have any solution for it. It probably lies overseas somewhere.

Thank you.

Mr. STENHOLM. Thank you, Mr. Mullins.

We will now hear from Mr. Buddy Baldrige of the National Association of Royalty Owners, Snyder, TX.

TEXTIMONY OF BUDDY B. BALDRIDGE, NATIONAL ASSOCIATION OF ROYALTY OWNERS, INC., SNYDER, TX

Mr. BALDRIDGE. Thank you, Congressmen Stenholm and Combest. Thank you for the opportunity to meet with you today to discuss the economic impact of the proposed tax reform and the current declining oil prices and natural gas on small business.

I am a Kent County rancher and fortunate enough to have a small royalty interest. Being a cattleman should qualify me for small business these days.

I come today representing the National Association of Royalty Owners [NARO], an organization for which I serve as a member of the board of governors and cochairman of NARO-Texas. NARO represents over 39,000 royalty owners in the United States, and was formed after the windfall profits tax was unfairly imposed on the Nation's royalty owners.

In November 1984, the Department of the Treasury, at the request of President Reagan, issued a proposal for income tax reform. The goals of this proposal, as stated in its introduction, were simplicity, fairness, and economic growth. These goals are admirable. However, none of the versions of tax reform that have been presented actually address or even achieve these goals.

For instance, simplicity. The proposals involve many more detailed calculations than current law, especially in the areas where inflation factors must be used. Even the simple calculation for personal exemption is complicated by inflation factors.

Fairness. The proposals are considered to be revenue neutral. Therefore, if the taxes of one group are reduced, some other group must pay the difference. Individuals will pay less tax, many will pay none at all, and business will have to pay more. The oil and gas industry is a target for higher taxes, even though they already pay more taxes than any other industry.

Economic growth. The shift of the tax burden from individuals to businesses will hinder rather than help economic growth. The increased tax burden will cause many businesses to close, eliminating jobs and economic activity. The best tax reform package would be no package at all.

The American Institute of Certified Public Accountants has recommended a 3-year moratorium on any tax law changes. This would give taxpayers, tax practitioners, and especially the Internal Revenue Service a chance to try to understand the tax laws that are currently on the books.

Oil and gas prices ended their creep downward in January 1986 and began to fall sharply. In a period of 2 months, oil has fallen from \$28-\$30 a barrel to \$11-\$13 per barrel, while gas has dropped off by a one-third and, in some cases, one-half.

Yesterday's spot market has already been mentioned, which dropped below \$10.

The effects of this drastic price drop will be felt by oil, and gas, and related industries, as well as local taxing authorities. Recent studies done by the National Association of Royalty Owners indicate that if an oil price drop of \$10 per barrel from \$26 to \$16 prevails for 12 months, Texas royalty owners will lose \$1.3 billion and the Texas economy will lose approximately \$4 billion. Royalty owners nationwide will lose \$6 billion, and the U.S. economy will lose \$18 billion. If the current pricing trends below \$15 prevail, these losses will be even greater than predicted.

Over two-thirds of this loss of this income will come in rural communities whose agricultural economics are already weak. Farmers and ranchers who have relied on royalty payments to keep their operations in the black will join the hundreds of their peers who will be selling out. All small businesses in rural areas, be they retailers, agribusiness, or energy related, depend on the strength of the local economy for their existence. The demise of the oil and gas industry and the agribusiness will cause many small businesses to close their doors.

Many Sunbelt banks, both State and national, are suffering. The small local banks feel the effects of the financial problems in their own areas. However, the large bank holding companies are also feeling the effects of the downturn in prices. These banks have millions of dollars in loans outstanding to energy, agribusiness, and foreign borrowers. The effects are already taking their toll.

Standard & Poor 2 weeks ago, placed six major Texas banks, including Republic Bank, Texas America Bank Shares, Inner First, Allied, and First City Bank on a credit watch. On Monday, the debt ratings on five of these were cut. Many of these borrowers are now in default on their loans and have no way to make payments. If these banks, both small and large have to close, the U.S. Government, through the FDIC, will have to pay off the depositors. The Federal Government already has enough debt of its own without having to add that of approximately 600 major banks in the Sun Belt.

Local taxing authorities that rely on ad valorem taxes for their income will lose over 50 percent of their assessed valuation because of the downturn in the oil and gas industry. Districts that rely on stripper and other marginal wells for their tax base will lose as

much as 75 percent because these wells will be closed when they are no longer profitable. Texas schools will lose approximately \$42.1 billion in assessed valuation, which amounts to approximately \$252.6 million in actual tax revenue loss. Taxpayers, many of whom are already having financial difficulties, will have to pay the additional taxes needed to keep the local governments and school districts operating. Again, the rural districts will be hit the hardest.

The Texas Comptroller of Public Accounts predicts that Texas will lose over \$100 million in income and 14,000 to 23,000 jobs for each \$1 per barrel drop in the price of oil. Using these figures, Texas has already lost \$1.6 billion in revenues and approximately 240,000 jobs since January of this year. Many businesses have closed and many more will follow.

What can be done to relieve the national energy problem and the economies of oil and gas producing areas? A reasonable, responsible national energy policy must be developed. The National Association of Royalty Owners, through its board of governors, has adopted the following five-point plan for the survival of the Nation's oil and gas producers and associated royalty owners.

First; Repeal of the windfall profits tax, effective January 1, 1986. When the price of oil falls below \$19.50 per barrel, the windfall profits tax no longer applies. Windfall profits tax was reasonably aimed at the major oil companies, but it unfairly included the royalty owners. The majors simply passed this tax on to the consumers.

Second, repeal the Industrial Fuel Use Act. This act discriminates against natural gas in favor of coal. Thousands of natural gas wells are being shut in because there is no market, while industries and utilities are paying to import coal from as many as five States away.

Third, total deregulation of natural gas. Natural gas is the only regulated commodity in the United States. Decontrol would allow the price of the gas to be controlled by the forces of supply and demand, and would allow royalty owners and producers to receive a fair price for their gas.

Gas wells drilled prior to 1978 are regulated and four-fifths of all natural gas royalty owners and producers are locked into regulated contracts that establish a price of 50 cents for Mcf and below, some are even as low as 13 cents for Mcf, while the prevailing market price is between \$2 and \$4 per Mcf.

Fourth, retain the deduction for intangible drilling costs. Exploration for oil and gas is an expensive operation. Operators should be able to deduct the cost associated with drilling and completing wells, just as other businesses deduct the cost of promotion and development.

Fifth, return percentage depletion to 27½ percent or capital gains treatment for royalty owner sale of oil and gas. Oil and gas are depletable, nonreplaceable assets. Once that is taken from the ground, there will be no more. To achieve the goals of fairness and simplicity, receipts from the sale of oil and gas should be treated like the receipts from the sale of any other asset on an installment basis and should be subject to capital gains treatment.

We ask today that you and your colleagues take heed of the devastating effects that the proposed tax loss, coupled with the sharp drop in oil and gas prices will have on local, State, and national economies. Independent producers drill approximately 90 percent of the wells drilled each year, and if they cease to exist, the price of oil and gas in the United States will reach new highs. We will continue to be held hostage by OPEC and the whims of Mideast rulers. The U.S. Congress must act to promote exploration and production of oil and gas and to prevent the extinction of the independent producers, royalty owners, and small businesses for the sake of our great Nation.

Thank you for your concern.

[Attachments to testimony follow:]

UNITED STATES HOUSE OF REPRESENTATIVES
SMALL BUSINESS ENERGY & ENVIRONMENT SUB-COMMITTEE
HEARINGS
ARILENE, TEXAS
APRIL 2, 1986

Testimony by Buddy Baldrige on behalf of
the National Association of Royalty Owners

SAMPLE TAXING AUTHORITY		1985 MINERAL	1985 OTHER	1985 TOTAL	PERCENT DECREASE	ADJUSTED TAX RATE *
APPRAISED VALUE		\$642,419,910	\$39,275,400	\$681,695,310		
PERCENT		94.24%	5.76%	100.00%		
1985 TAX	0.2545	\$1,634,959	\$99,956	\$1,734,915		
AT \$25/BBL TAX		\$553,010,267 \$1,620,025	\$39,275,400 \$114,090	\$593,005,667 \$1,734,915	13.79%	\$0.2925
AT \$20/BBL TAX		\$443,040,214 \$1,593,641	\$39,275,400 \$141,273	\$482,323,614 \$1,734,915	31.03%	\$0.3597
AT \$15/BBL TAX		\$332,286,160 \$1,551,528	\$39,275,400 \$183,387	\$371,561,560 \$1,734,915	48.28%	\$0.4669
PERCENT		89.43%	10.57%	100.00%		
AT \$12.50 TAX		\$276,905,134 \$1,519,406	\$39,275,400 \$215,508	\$316,180,534 \$1,734,915	56.90%	\$0.5487
PERCENT		87.58%	12.42%	100.00%		

STATE PROPERTY TAX BOARD REPORTS THAT THE
1985 TOTAL OIL, GAS, AND MINERAL ASSESSED VALUE
TEXAS SCHOOLS- \$84,224,652,349

ASSUME A 50% DECLINE
\$42,112,326,175

AVERAGE SCHOOL TAX RATE
\$0.60

TAX REVENUE LOSS \$252,673,957

* NOTE: The adjusted tax rates are the rates that
would be needed to maintain the same level of revenue.
The need for additional revenue would cause an increase
in these rates.



**CRUDE PRICE DROP IMPACT
ON ROYALTY INCOME**

Alabama	-\$ 28.2 million
Arkansas	-\$ 28.3 million
California	-\$720 million
Colorado	-\$ 43 million
Florida	-\$ 15.6 million
Illinois	-\$ 43.7 million
Indiana	-\$ 6.9 million
Kansas	-\$112 million
Kentucky	-\$ 11 million
Louisiana	-\$740 million
Michigan	-\$ 48.1 million
Mississippi	-\$ 49 million
Montana	-\$ 45 million
New Mexico	-\$116.4 million
New York	-\$ 1.5 million
North Dakota	-\$ 77.3 million
Ohio	-\$ 22.3 million
Oklahoma	-\$270 million
Pennsylvania	-\$ 6.2 million
South Dakota	-\$ 1.4 million
Tennessee	-\$ 1.3 million
Texas	-\$ 1.3 billion
Utah	-\$ 45 million
Wyoming	-\$146 million

Footnote: The above data was compiled from 1984 production records of World Oil on a per barrel basis. The royalty computation was set at 15 percent as a weighted average of common royalties of 1/8th, 1/6th, and 3/16ths. The base computed was from \$26 per bbl oil to the existing West Texas barometer of \$16. Farm-ranch operations -- on an average account for a minimum of 1/3rd royalty recipients, rural areas another 1/3rd with the remainder, due to assignments and migration, urban or retirement area dwellers. For economic impact determination in rural areas, the multiplier of 3 is often used. NARO surveys show the average royalty owner of oil or gas at or in retirement (over 65) and surviving on run checks of \$200 or less except in select parts of the nation (W. Texas) where an average \$345 is the norm. There are an estimated minimum of 2.5 million royalty owners of oil and gas interests in the nation.

Reason: Security is the No. 1 responsibility of the Federal Government...

AMERICA'S DEFENSE MUST NEVER BE COMPROMISED

...yet the U. S. Treasury's plan to purposely reduce American oil drilling and production, and their conclusion that America should depend on supplies of foreign oil could devastate U. S. national security!



"I KNOW, GENERAL, I KNOW! BUT WE'RE STILL WAITING FOR OUR IMPORTED FUEL TO GET HERE!"

U.S. TREASURY TAX PLAN ENDANGERS NATIONAL SECURITY!

A proposal to replace American oil with more Middle East imports puts U.S. safety in hands of desert sheiks



"The Golden Age of Arab oil was not in the seventies but will be in the nineties of this century"

—James A. Baker, Jr., Secretary of the U.S. Department of the Treasury

♦ IT'S NOT A PARTY ISSUE ♦ THE LAW DEMANDS

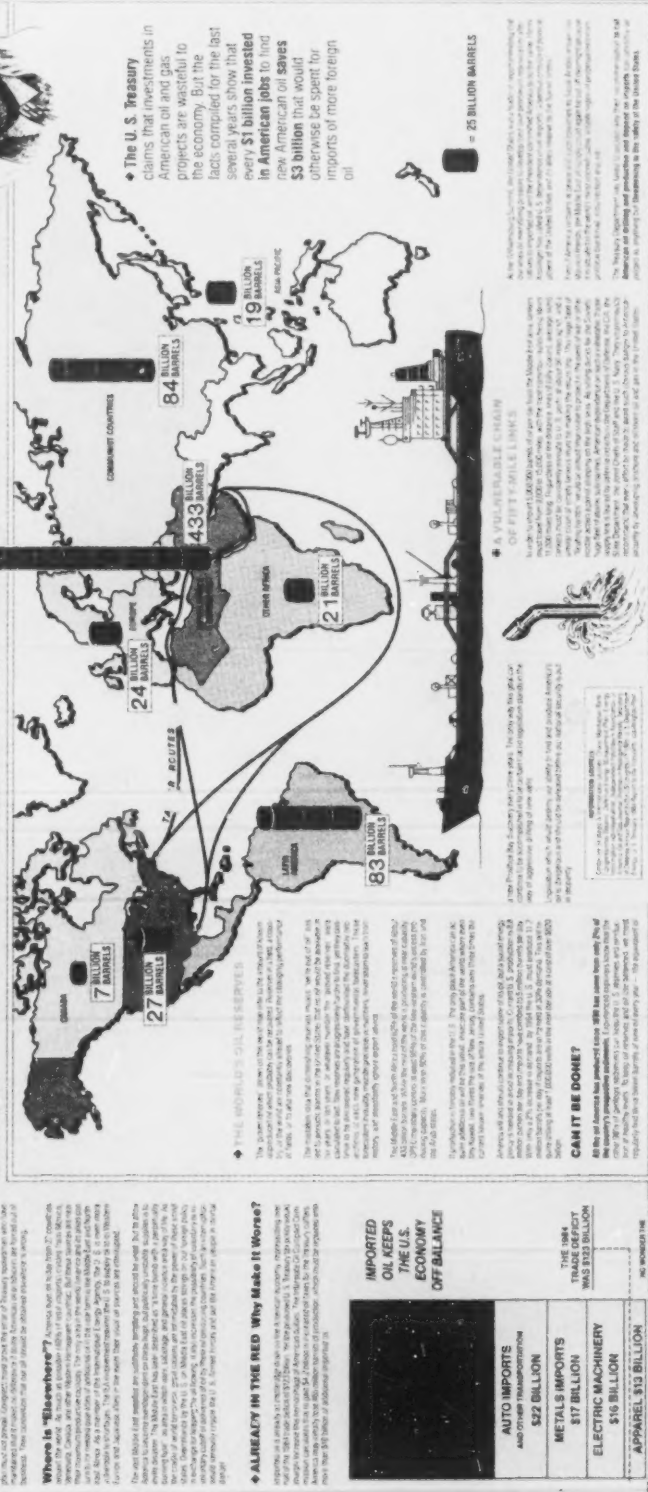
The Treasury's oil policy is not a party issue. It is a matter of national security. The law demands that the Treasury must take steps to ensure that the United States has a secure and adequate supply of oil. The law also requires the Treasury to report to Congress on the progress of its efforts to meet these obligations.

♦ THE WORLD'S OIL RESERVES ♦

The world's oil reserves are being depleted at an alarming rate. The United States has the largest reserves, but they are being used up much faster than we think. The world's reserves are being used up much faster than we think.

♦ WHERE IS "BLACKHOLE"? ♦

The world's oil reserves are being depleted at an alarming rate. The United States has the largest reserves, but they are being used up much faster than we think. The world's reserves are being used up much faster than we think.



U.S. DEPARTMENT OF THE INTERIOR, GEOLOGICAL SURVEY, 1980. THE U.S. DEPARTMENT OF THE INTERIOR, GEOLOGICAL SURVEY, 1980. THE U.S. DEPARTMENT OF THE INTERIOR, GEOLOGICAL SURVEY, 1980.

WHEN THE OIL AMERICA NEEDS IS CONTROLLED BY SOMEBODY ELSE, THEN SOMEBODY ELSE CAN CONTROL AMERICAN DEFENSE DECISIONS

The U. S. Department of Defense is the nation's largest consumer of petroleum even in peacetime, and petroleum use is projected to quadruple in the event of war. Tanks, airplanes and ships of today's military forces, and weapons systems on the drawing board, all operate only on liquid petroleum. In 1964, 63% of all the petroleum purchased by the military was used for mobility of defense materiel.

It hardly be an unarguable oversight to award hundreds of billions of American tax dollars for the finest defense machines ever seen on land, sea, and air, and then fail to be absolutely certain that we have adequate, ready and reliable fuel supplies to ensure their operation. Without petroleum, U. S. Army vehicles remain parked, U. S. Navy ships stay docked and U. S. Air Force planes do not fly.

Domestic American Oil must always be available for the nation's defense. Over 15 years are required to bring a newly discovered oil field into full production. Unless oil is produced continuously, and aggressive exploration continues to replace dwindling American reserves with new discoveries, the U. S. oil industry will be strangled into rusty, inefficient ineffectiveness. It will be unable to provide emergency supplies of oil when they could be most urgently needed for the protection of Americans. American security efforts demand measures for maintaining and increasing U. S. oil production.

The U. S. Treasury has wrongly argued that American oil is "no longer needed," and has proposed that investments in American oil production be forcibly reduced. They have concluded that America should be dependent on "other sources" for oil. But even such friends as Canada and Mexico have restricted petroleum exports to the U. S. In the early 1970's, Middle East producers used embargoes to retaliate against U. S. policy. The best prophet of the future is the past, and the threat of oil cutoffs to mold U. S. foreign policy should not be permitted again.

An Oil-Dependent America would be virtually paralyzed by simply cutting the wires to our national lifeline of oil. Plans like, or similar to, the Treasury plan are patently damaging and dangerous to the nation's defense posture. Any tax plan which tends to reduce the number of wells drilled for new oil and gas should be rejected by the Congress.



Mr. STENHOLM. Thank you, Mr. Baldridge.

Mr. COMBEST.

Mr. COMBEST. Thank you, Mr. Chairman.

Mr. MULLINS, do you do any exploring?

Mr. MULLINS. Yes, sir.

Mr. COMBEST. You say you are currently operating 25 wells?

Mr. MULLINS. Yes, sir.

Mr. COMBEST. How does this average in your time in business as far as—how is this as far as the average, is that more or less than you normally run, or do you try to set a level of about—

Mr. MULLINS. No; I have produced a few more than that. But 25 wells is just about what I operate mostly.

Mr. COMBEST. And it is a family operation, you and your son-in-law?

Mr. MULLINS. Son-in-law, yes, sir.

Mr. COMBEST. And those wells are averaging 1½ barrels a day?

Mr. MULLINS. Yes, sir.

Mr. COMBEST. I was impressed with your testimony because I think it will be extremely good to have that in the record. I believe a lot of people look at a Texas oil producer in terms of a J.R. Ewing. The fact that you are definitely running a small business, a family operation, yourself, that you do the work yourself, puts a little different perspective on it.

Now, I know there are, of course, many others that run operations like you do. You are running stripper wells, and you are running wells—I believe you used the figure of somewhere around \$20—that if oil is not at somewhere around \$20 may have to be plugged?

Mr. MULLINS. \$18 to \$20, in that area.

Mr. COMBEST. In testimony yesterday, Congressman Stenholm was trying to reach a specific figure. He asked people to comment specifically as to what they thought oil would have to reach for these plugged wells or wells, if they were plugged, to ever be reopened, stripper wells. Though there was not a real consensus, it was certainly a lot higher than that figure—\$20. Some people said \$60, some said \$80.

This is extremely important when you consider the fact that we receive so much of this Nation's supply of oil from stripper wells and that they are in such a situation. I think the market opened yesterday at \$9.90. It is a little higher today, but not nearly high enough. It is about half of what it has to be for you to be able to stay in business.

I do appreciate your testimony because, again, I think there is a real misunderstanding of what an oilman is like.

Mr. MULLINS. I think you are right. Most of the people around Olney, most of these wells around Olney range from 700 to 3,000 feet. Most of the people there operate their wells like I do, and most of them are hard hit. I would say half of them have already shut their wells in.

All of these wells—I do not want to mislead you—all of these wells might not be shut in. I have 1½ barrels average. Some of them do not make a barrel. Some of them make a little more than 1 barrel. The first to be shut in will be the ones that make less. You are also controlled by how much water you make. If you have

a lot of water, you just cannot handle the water. Your electric bill eats you alive. And there is a certain portion of these wells that I have already shut in. They are not producing today.

Mr. COMBEST. One of the impacts that I hope we are able to bring out in this hearing, and I appreciate it, is the fact that the chairman read in the letter. We are trying to look at this in terms of not just how the producer is affected. It is how all the support industries, it is how this motel in Abilene, TX, is going to fare under this problem.

I spent most of yesterday afternoon in Andrews, TX, looking at two large fields; a field that is producing for Amoco and a field that is producing up there for Exxon. The thing that was significant to me, one of the important things I think that was pointed out and that we discussed was that the people that are pulling the wells, the people that do the work on them, the people that are doing drilling on them are the ones out of work. They don't have any work. Amoco has shut down a number of wells. Exxon at this point has none out there. But, they are not doing any work, and they are not doing any more drilling. And this is the effect that it's really hitting home in these smaller towns, they are people out of work because nothing is being done in the industry.

Amoco and Exxon do not want to see this happen. They have a deep place in their heart for these workers, but that is the concern I think we have to look at. How does it affect all of these other small businesses, not just the producer himself?

Mr. MULLINS. The small businessman in Olney is hurting as bad as the small operator.

A friend of mine drove through Olney the first of this week and he counted the businesses that were closed on Main Street. And there were 15 businesses closed on the Main Street of Olney, and most of these were open a couple of years ago.

Mr. COMBEST. Thank you very much.

Mr. STENHOLM. For the record, let us go a little further into these 25 wells you are producing and the fact that it takes \$18 to \$20 to justify their continued operation. Obviously, at \$9.75 for oil, you are not going to produce them for very long.

What is the first step you take when you make a decision that it is uneconomic to continue operating a well?

Mr. MULLINS. Well, the first thing you do is just go out and throw the switch and just turn them off.

Mr. STENHOLM. Then what?

Mr. MULLINS. Well, if you do not produce anything that month, the Railroad Commission won't issue you an allowable for the next month. And probably I will produce them 1 or 2 days out of the month for awhile to keep my allowable. If the price did go up, if I didn't have an allowable, I would not be able to produce my wells. So I am sure that for awhile I will produce them 1 or 2 days out of the month to keep my allowable.

Also, if you shut them down for as much as 90 days, most of these leases go back to the landowner, and then you have a plugging job. So I am going to try to, as long as I can, I am going to try to produce them a little bit each month.

Mr. STENHOLM. What is your cost to plug a well?

Mr. MULLINS. A shallow well, probably a minimum of \$750 to a maximum of—say a 3,000-foot well, probably a maximum of \$2,500. And most of these you do not recover any casing. It is just cemented, from top to bottom, most of them are just a dead expense.

Mr. STENHOLM. Once a well is shut in, what is your estimation of the price that would be required to reenter that well and begin producing again?

Mr. MULLINS. Well, most of these shallow wells that I operate, you would not reenter them. You would probably be better off to step over from them and drill another well. And at today's cost, you're talking about, by the time you drill it and complete it, \$25,000 per well.

Mr. STENHOLM. Do you have any figures on the proven reserves of the amount of oil left in these 25 wells that you are talking about? What will be lost if you have to plug them?

Mr. MULLINS. I do not have the figures on that. I can tell you that some of these wells, since I have had them, have averaged the same amount of production for the last 10 years, and some of them have been producing since 1929. And they have been producing, within 1 barrel, say—I have six wells that have been producing within 1 barrel of what they were producing in 1975. So I have every indication to believe that they will be producing that way 10 years from now. They are all settled production, and they pretty well have been producing the way they're producing now for several years.

Mr. STENHOLM. Mr. Baldridge, does your association have a position on the question of an oil import fee?

Mr. BALDRIDGE. Yes, sir, we do; we support that as long as it is a clean import fee and does not exempt everybody in Canada and Mexico. As long as it is a clean bill, yes; anything we can do to back up our price, we would be in favor of. Yes.

Mr. STENHOLM. I think in both of your testimonies you acknowledged and recognized that there are no immediate quick-fix solutions to the problems that befall us. You recognize very correctly that the future of the energy business in the United States is out of our hands today. It is now in the hands of someone else. This morning's Abilene Reporter-News indicates a recognition now, from the President on down, that oil price control is centered in the Mideast and particularly in Saudi Arabia.

We remember the good old days in Texas when it was the Texas Railroad Commission that controlled world oil prices. I think we are having difficulty now accepting the fact that this control has slipped from us in Texas and the United States. We are now dependent upon another region for what could very well be our economic and national security at some point in time, if we don't reach some answers. I think both of you have indicated that.

I agree, and I know Mr. Combest does also, with the five points that you mentioned in your testimony. I think you will find substantial agreement for these proposals among the oil patch representatives. You will find substantial disagreement with those in the other 45 nonproducing States.

Mr. BALDRIDGE. I think one good point in the handout that is attached to the statement, which the Pitts Energy Group worked up; one of the oil ministers from Saudi Arabia—and I cannot pro-

nounce those names. His quote is that the golden age of Arab oil was not in the 1970's, but will be in the 1990's in this century. They are looking—and I think they are right—at some point in time, when the market cleans up, the price of oil is going to get out of sight and we are going to be the ones paying for it. Their statement was that it would take—on an 11,000-mile trip from Saudi Arabia to Houston, it takes a tanker every 50 miles, both directions, to supply the 5 million barrels that we are importing now from South America. And that figures out to 440 tankers. That stretches my imagination just a little bit.

Mr. STENHOLM. Mine, too; and that is a good point for us to consider.

It is always difficult to deal with national policy on anything. During the hearing yesterday, there was a recognition coming from the oil industry and from within the administration that there is no such thing as a free world market. There is certainly not a free world market in oil and gas production today. Somehow, we have got to accept that fact and implement appropriate policies.

Thank you for your testimony. We appreciate very much your participation in this hearing. Thank you for your contribution.

I next will call panel two. We will hear from Dr. William L. Fisher, director of the Bureau of Economic Geology, University of Texas, Austin, TX, and Doug Williamson with the Abilene Reporter-News here in Abilene.

Dr. Fisher, please begin.

**TESTIMONY OF WILLIAM L. FISHER, DIRECTOR, BUREAU OF
ECONOMIC GEOLOGY, UNIVERSITY OF TEXAS, AUSTIN, TX**

Dr. FISHER. Thank you, Mr. Chairman. I am very pleased to be here.

I have provided to the subcommittee more extended remarks, but, if I may, I will simply briefly and orally summarize my main points at this time.

Mr. STENHOLM. Your entire statement will be made a part of the record, and we would appreciate a summarization.

Dr. FISHER. Thank you, Mr. Chairman.

Your letter of invitation expressed your very real and deep concern on the fate, likely fate of many of the independent or small oil and gas producers and explorers. I think that concern is exceedingly well taken. If the prices we are experiencing now persist for a good while, and I think that there is very good likelihood that they will absent any kind of action in the United States, the days of many of our independent producers are really numbered.

Whether the aim by the Saudi Arabians to make deliberate overproduction and oversupply in the world is to knock out marginal production capacity, or higher cost production, or not, that will certainly be the consequence of their action if these prices persist for any particular time. And we have to appreciate that within the world, the United States holds the bulk of the higher cost production. And much of that is in the hands of the independent operators. The principal exploration targets for oil and gas, which is affected by these lower oil prices, are primarily moderate- to small-size fields. And, again, it is the area of exploration conducted large-

ly by independent operators. So both the production and the exploration side get hit.

We will have the impact of this lost production throughout the entire United States, but some areas will get hit much harder than others. My own estimates, as I told a previous committee of the Congress is that by 1990 prices at \$15 will knock out about one-third of the oil and liquid production capacity in the United States. That much is at risk over that 3-year period. And that, of course, Mr. Chairman, with any kind of an increase in demand would put us back into an import situation in this country at the heaviest points we were in the 1970's, and impose that we relive the whole economic dislocation that we saw in the 1970's as we wrestled through the energy crisis.

One of the areas that gets impacted hard, and I know you are very conscious of it, is stripper oil production. In Texas, 70 percent of all the wells are strippers. They produce 10 barrels a day or less. These are all over the State, but they are concentrated in some parts of the State. If you take, for example, what we call the eastern shelf is the Midland Basin, which is Railroad Commission districts 9 and 7(b). Abilene sets within that area. This is a bailiwick of independents and small operators, and has been for a long time. The percent of stripper wells is not 70, as it is statewide; it is 90 percent—90 percent of all the wells.

If you look at small stripper wells, by that, making no more than 3 barrels a day, 70 percent of the wells in this part of the country are in that category, compared to about 45 percent throughout the State. And if you look at what we call the very small strippers, that is, wells making less than 1 barrel a day, nearly half of the wells in the eastern shelf of the Permian Basin are in that particular category.

And of the total volume of production here almost half, 43 percent of all the crude oil production in the eastern shelf, is from stripper wells.

I project that the U.S. stripper production lost at \$15 a barrel will be on the order of something about 400,000 barrels a day of capacity. And that will occur over the next few months. Some of it is going on now. Texas will absorb about 150,000 barrels a day of that loss, and 30 percent of the entire Texas loss is going to be seen here in this part of the country in the eastern shelf because of its high orientation toward stripper production.

Statewide, this kind of a loss for us will be about 6 percent of total production. But in the eastern shelf, the Abilene area and on up to Wichita Falls, the production loss at \$15 from stripper wells will be 20 percent of total production. You are making massive inroads into the production capability of this part of the world with that knockout of stripper wells. And that is simply eliminating only those wells that are making 3 barrels a day or less. Some that are making a little bit better than that, if they are cutting a lot of water, can be in that category, too.

We project, also, Mr. Chairman, that natural gas drilling and liquid separation activity will also decrease. There will be a loss of about 400,000 barrels a day of liquids capacity. Independents that are involved in gas exploration will suffer along with the rest in that category.

In Alaska, which we must mention as a part of the whole national impact, we will see a loss of about 700,000 barrels a day of production capacity by 1990 at \$15 prices. Prudhoe Bay is scheduled to go into decline at about 12 to 15 percent in 1987. There is additional production capacity on the North Slope that could back that out, but not at \$15.

Also, we expect something on the order—in fact, we have already seen this announced by most of the major operators—of at least a 30-percent decline in drilling activity due to reduced internal cash-flow or, in the case of the independents, the inability to attract drilling funds.

Overall in the United States, we are estimating that about 3 million barrels a day of capacity of liquids and crude will be knocked out by 1990. Texas will see about 885,000 barrels of that per day of that capacity loss.

Now, let me turn beyond just the production impacts, which are very, very substantial. We will move to one other point, and that is the exploration prospects that we have.

We are in what I refer to as stage 3 exploration in the lower 48. We have gone through the discovery of the big fields and we have gone through the discovery of a lot of the intermediate size fields. What we are now exploring for the most is a very large number of very small size fields; 98 percent of all the fields discovered over the last 15 years in the United States have been less than 1 million barrels of oil or gas equivalent. A lot of them are one-half million barrels or even less.

The very positive part of that is that there are many tens of thousands of these small fields, and they are pursued largely by independents. There is relatively small overhead, ideally suited to independent operators. And that is why you see independents drilling so many of the wildcat and exploration wells. That is why we have seen some of the rough and tough restructuring over the last 5 and 6 years, as the whole corporate area in oil and gas tries to restructure to this smaller target resource base. We are down now to where we add reserves in increments of a one-half million barrels rather than by billions.

Throughout most of the 1970's, we were finding in the United States about 250 of these small to modest fields per year. That shot up with the higher prices to better than 1,000 smaller fields per year, mostly found by independents. It will drop down at \$15 to well below 400. So the impact and the ability to put together deals on these smaller type prospects, which are quite economical in the \$25 to \$30 range, will lose out substantially at \$15 or below.

Mr. Chairman, with the loss of the U.S. production capacity and even with a modest increase in demand, we will see by 1990 a situation in which we will be importing 8½ to 9 million barrels a day, as much as we did in the late 1970's. And we will be poised, I think, to relive the energy and the economic dislocations that we had in the 1970's, and probably even worse.

What to do? I think we are in a situation of relatively low prices for a period of as much as 3 or 4 years if we do not do anything about it. And the reason for that I believe is that there exists no longer anyone in the world willing, or even maybe anyone capable of assuming a swing producer's role. The Saudi Arabians have done

that for the last 4 years, bringing their own production down from about 10 million barrels a day to close to 2 million. And they saw themselves rapidly moving into a situation of zero market share. And so, quite arguably, one can make a case that the Saudis did what they did largely because they really did not have much of a choice and had very little to lose by doing it.

That indicates to me that we are dealing with a structural collapse of the capability to administer a price at a stable level.

There are several things we can do to alleviate the situation. Many have been mentioned in previous testimony: Repeal of the windfall profit tax; certainly repeal the Fuel Use Act. I cannot imagine how this thing has lagged on as long as it has. Everybody seems to be opposed to it, but it is still on our books, Mr. Chairman, as you very well know. Also, the deregulation of natural gas; that is probably one you want to approach with a little bit of phasing. It is a long-term thing that needs to be done, but there could be some discontinuities there if it is not looked at carefully. Certainly maintain the provisions of the Tax Code which have been very significant and very important to enable us to pursue the marginal end of the resource base, the small field exploration and the like. And if we lose that, that will be a very detrimental fact.

But all of those things together is not enough to stop the hemorrhaging that we are having at the present time. I think that absent a swing producer or a residual supplier in the world, someone willing to do that as we did that in Texas for 30 or 40 years, and the Saudis did for about 4 years, there is no one else on the scene that can serve the role or will serve the role as a swing producer to be able to adjust the supply to the demand at such level that you can stabilize the price. We have to play the role in the United States as a stabilizer. After all, in terms of oil and gas in the free world, we still produce 30 percent. We consume 40 percent of all the free world's oil and gas. We are the major player by any stretch of the imagination, not necessarily the Saudis. The Saudis are the biggest holder of low-cost oil; there is no question about that. But we play a very major role.

What we should do is, I think given the fact that I see very little likelihood of the OPEC being able to administer a price at a stable and at an appropriate level for us, take unilateral action in this country. And that is the imposition of an import tariff fee, a variable one that slides down, that allows us to maintain a price in this country that is sufficient for us to add reserves. We must act if we want to be able to keep production at a relatively stable level, to keep our levels of imports in the 30- to 35-percent range, which is a very manageable one, as opposed to 50 or 60 percent where you have exceeding vulnerability and very little control of the situation.

If we want that, there is a very ample resource base out there. It is in small increments, it is in marginal increments. And we are going to have to pay more than what the Saudis can do with the price. Half the oil in the world can be lifted for less than \$3 or \$4. All of that is in the Persian Gulf. If the amount of oil that we have, if we talk about replacement of reserves, we are talking \$20 to \$25, even \$30 for most of the kinds of reserves that we want to replace in this country.

I submit, Mr. Chairman, that range is as much in the order of magnitude in the intrinsic value of oil. It is almost impossible for a classic free market to function in that kind of a situation unless one country controls all that range, which we do not. We are concentrating on the marginal end. That low-cost end is what we no longer have. We used to have it 30 and 40 years ago; we do not have it now. We have to take it into our own hands, I think, unilaterally, and do so until such time as there is a capability internationally or worldwide to stabilize a price that is consistent with what we have to do to maintain a sufficient level of production in this country.

Thank you, sir.

[Dr. Fisher's prepared statement, with attachment, follows:]

PREPARED STATEMENT OF WILLIAM L. FISHER,
DIRECTOR, BUREAU OF ECONOMIC GEOLOGY,
UNIVERSITY OF TEXAS, AUSTIN, TX

I

In the Chairman's letter of invitation, he expressed concern about the severe economic setbacks independent oil and gas producers are experiencing. Such concern is well taken because if the present situation exists for much longer, as it is likely to do absent appropriate action, many independent oil and gas explorers and producers have their days numbered.

The action early this year by the Saudis to drive down oil prices and to recapture, for them, a share of the world oil market, appears to have been aimed primarily at the world's higher-cost, or more marginal, oil production, and that is chiefly in the U.S. and inordinately held by the U.S. independents. Not only is the U.S. the world's largest producer of higher-cost oil, but a very large part of the oil available for reserve replacement is also high-cost, at least relative to the very low-cost oil of the Middle East.

II

Let us look at what oil prices in the \$15 range will do to production capacity in the U.S., in Texas, and more specifically, within the independent sector.

In the U.S., there is a large volume of production coming from wells with a low daily yield. In Texas, a good representative of the U.S. Lower 48, more than 95 percent of all wells produce less than 50 barrels per day, and about 70 percent of all wells, the so-called

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stripper wells, produce 10 barrels a day or less. Obviously, production from these low-yield wells is very sensitive to price. In the U.S. a total of 1.3 million barrels per day is produced from about 450,000 stripper wells. About 400,000 barrels a day come from wells producing only 3 barrels per day or less. At \$15, the great bulk of these wells and a significant number of other more costly stripper wells will be plugged and abandoned. In excess of 400,000 barrels a day of capacity will be lost over the next 12 months. If prices were to fall to \$10, the loss would be closer to a million barrels a day.

The loss of stripper well production impacts heavily the small operator. Let's take the Eastern Shelf of the Permian Basin, on which Abilene sits. This area has long been a major operating area for independents. While statewide, wells making 10 barrels a day or less represent 70 percent of the total wells, in this area nearly 90 percent are strippers. Statewide low-yield strippers, 3 b/d or less, are 45 percent of all wells; in the Eastern Shelf 70 percent of all wells produce 3 b/d or less. And to further illustrate the sensitivity, nearly half of all wells on the Eastern Shelf, or more than 20,000, make 1 b/d or less. Some 43 percent of all Eastern Shelf production comes from stripper wells, a percentage well over twice the State or National percentage. At \$15 prices, Texas will lose 150,000 b/d of stripper capacity within 12 months, and more if prices fall further. Of Texas' total lost stripper production, Abilene and the Eastern Shelf will absorb nearly 30 percent of the loss. Loss of stripper capacity at \$15 will cost the State about 6 percent of its production; this area will lose nearly 20 percent of its total production.

Severely reduced cash flow at \$15 per barrel will reduce oil drilling drastically, both for reserve growth and new-field discovery, yielding a corresponding loss of reserve additions. While additions nearly equaled production over the past five years, the reduction in drilling at the \$15 price will result in a Lower 48, nonstripper production decline of about 5 percent annually, essentially the decline level of the 1970's. This translates to a production loss of 1.6 million barrels per day by 1990, and nearly 3 million barrels per day by 1995.

Some 560,000 b/d of this volume will be lost in Texas by 1990, and by 1995 nearly 1 million b/d, or 40 percent of current capacity. A major part of this lost capacity will be due to lack of additions from severely reduced field drilling, and since about 80 percent of this kind of reserve growth is in North and West Texas, this area will absorb a major part of the loss. Lower oil prices will further depress natural gas prices with corresponding declines in gas drilling and production capability, and with increased interfuel competition, could also decrease gas demand. Nationally this will result in a loss of about 400,000 b/d of natural gas liquids by 1990. Texas will absorb about 175,000 b/d, of that loss.

Alaskan North Slope production, now 1.7 million barrels per day and chiefly from the Prudhoe Bay Field, is scheduled to go into normal decline in 1987. An annual decline rate of between 12 and 15 percent is anticipated. This will reduce Alaskan North Slope production to about 1 million barrels per day by 1990, and to 600,000 barrels per day by 1995. While about 1 million barrels a day of additional capacity exist in already discovered, smaller fields on the North

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Slope, production and transportation costs will make this capacity uneconomical at \$15 per barrel, and little or no back-out of Prudhoe Bay decline is anticipated.

I estimate the total production impact on crude oil and liquids to be about 3.1 million b/d by 1990 if \$15 prices persist. Texas will lose an estimated 885,000 b/d of capacity by 1990, 28 percent of the total U.S. loss and about 37 percent of total Lower-48 liquids capacity loss.

III

Aside from the knockout of current production capacity, \$15 oil will have an enormous impact on exploration and development. We have a very substantial capability to add reserves through discovery and intense development, significantly better capability than we were judged to have just 10 years ago. The fact that production declines in the Lower 48 during the 1970's have been flat arrested since 1979 is ample proof of that capability. That capacity exists, however, in increments of discovery and reserve growth that are small, not huge, and that require an intensive level of drilling, both discovery and development, if significant volumes of reserve are to be added.

While large-field discovery still occurs in the U.S., it is relatively infrequent and concentrated in deeper offshore waters and in the Arctic. The bulk of discovery is now in small and modest-sized fields, less than 10 million barrels in size, but much more commonly less than 1 million barrels. While the negative side is that we are exploring for small and modest-sized fields almost entirely, the positive side is that we now judge that there are tens of thousands of

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such fields and that they contribute a stable, if low, rate of finding. I estimate that total discovery of oil and gas in the U.S. will amount to about 430 billion boe, of which 35 percent is yet to be discovered. While two-thirds of the oil and gas discovered to date has been in fields of 25 million barrels or more, two-thirds of future volume to be discovered will be in fields less than 10 million barrels in size, and most in fields less than 1 million barrels in size. Future discovery, for the most part will come in small increments, requiring substantial levels of drilling if significant volumes are to be added. In my judgment, there are a sufficient number of small and modest-sized fields to support a level of exploration comparable to that of the past six years for at least another 40 years. But small field exploration generally lacks the economy of scale; it must be pursued with low overhead, and that is why such objectives are generally drilled by independents. In the late 1960's and early 1970's we discovered about 250 small and modest-sized fields per year in the U.S. In the early 1980's nearly 1,000 such fields were discovered annually. The remarkable increase was due to higher prices which allowed these objectives to be economic. At \$15 the annual number of small field discoveries that will be economic will fall to 400 or less, and at least one-third of the reduction will occur in Texas. Independents throughout the U.S. will feel the brunt of it.

IV

If there is no increase in consumption of oil and liquids in the U.S. through 1990, not likely with low prices, our level of imports by 1990 will match the highest level in history achieved in 1979. If

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there is even modest increase in demand, that level, of course, will be exceeded. If low prices were to persist through 1995 and there were little or no increase in demand, two-thirds of demand would come from imports.

v

We are, with low prices, poised for a repeat of the 1970's on the production side, except unlike the 1970's, we have no major Alaskan source coming on line.

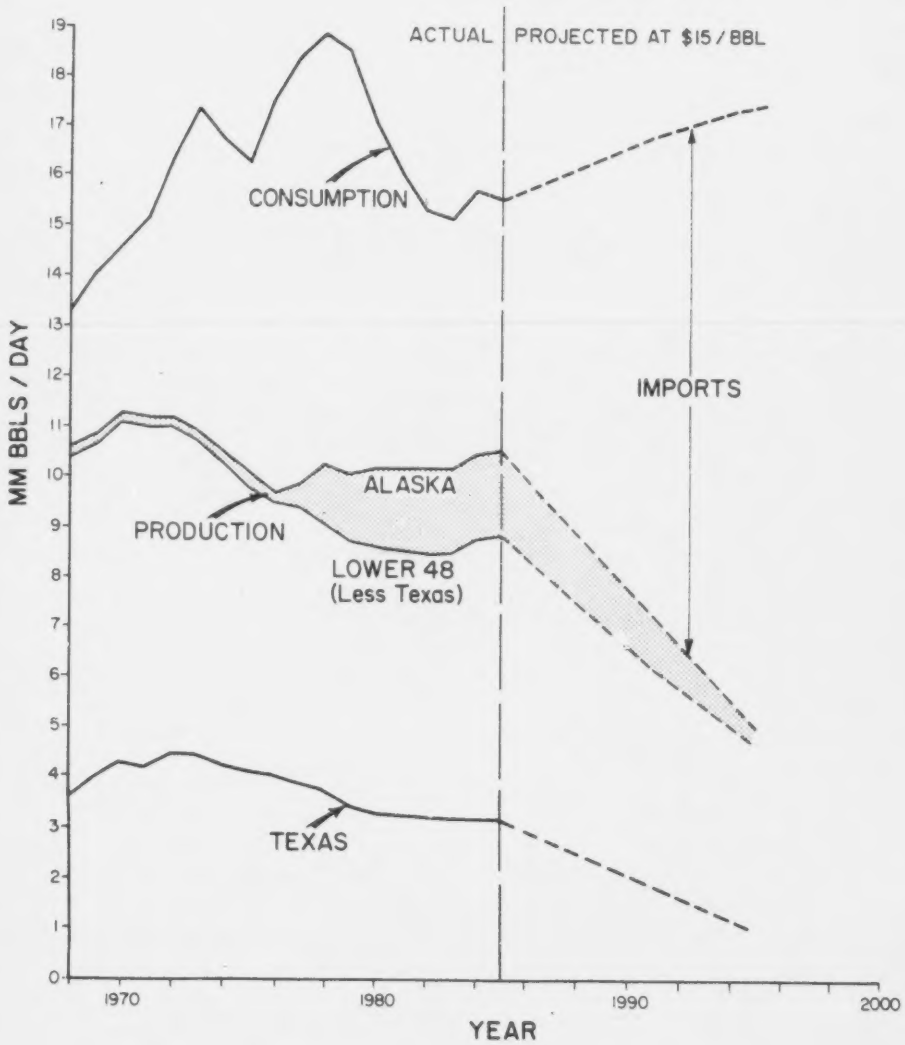
Lower prices of oil, while negatively impacting the U.S. producing states, will have a positive impact overall, in the short run. The real question, in my mind, becomes, Shall we accept the economic benefits of today for the certain impact of acute dependence tomorrow, or do we want to maintain a price level sufficient for reserve replacement in this country and with it relatively stable production levels and a manageable volume of imports?

In my judgment, it is essential that we conduct oil and gas exploration and development programs in the Nation sufficient to supply about 65 to 70 percent of our petroleum needs. Recent experience is that such was accomplished with oil prices that existed over the past five years. I see little prospect of the OPEC and the other producing countries balancing supply and demand to provide such a price level, simply because administration of a supply and demand balance on a collective basis is without historical precedence. To avoid heavy import dependence and to avoid a repeat of the severe economic dislocations of the late 1970's, the U.S. must protect its oil and gas production capability, and the preferred mechanism would be some sort

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of a variable or sliding fee on imported oil and oil products. The objections to such an approach as well as the desire to enjoy short-term price advantages are substantial, but they pale to insignificance compared with reliving energy problems as severe as those of the 1970's and probably worse.

U.S. OIL AND LIQUIDS—PRODUCTION AND CONSUMPTION



Mr. STENHOLM. Thank you, Dr. Fisher.

Now We will hear from Mr. Doug Williamson, with the Abilene Reporter-News in Abilene, TX.

TESTIMONY OF DOUG WILLIAMSON, BUSINESS EDITOR, ABILENE REPORTER-NEWS, ABILENE, TX

Mr. WILLIAMSON. Thank you very much.

I am very honored by this invitation, and will try to give you a picture of what the economy is like here in Abilene and the Big Country. Usually, the only invitation that a reporter gets is to leave the room, so I am very honored by this. Thank you very much.

I would like to paint a very optimistic picture for you, but I cannot, because it is just not out there at this time. Since the emergence of OPEC in the 1970's, petroleum has been somewhat of a shaky leg on our economic milk stool here in Abilene in the Big Country. It has had its ups, it has had its downs, and today it is down and is really down.

Unfortunately, the other two legs our economy sits on here, both the military and agriculture, are somewhat a little bit shakier than they have been in the past. Agriculture has been off and on in the past. And right now the military is not quite as strong as we wish that it was here in Abilene.

Local oil men publicly claim that they are not scared of the price-busters out on the New York Mercantile Exchange or over in OPEC and other markets around the world. We have quoted them several times in our paper, saying that is just the folks up there in New York and over in the Middle East, and its futures prices; that really does not mean too much to us here. We are getting what we are getting today. Unfortunately, what we are getting today is what they said a few months ago.

However, privately, some of our oil men are shaking in their boots. Their inherent west Texas conservatism has moved even farther to the right. They are taking a highly cautious approach to operations. Many of them have cut back drastically. They are in the mom-and-pop mode, as I like to call it, using family for office staff and secondhand pipe out in the field.

They need to be shaking, however. We have little if any control over the situation. The OPEC cartel has us by the throat. One university professor here in town, who closely tracks the Abilene economy, told me last week that those people who are optimistic about the situation right now are going to be disappointed. It all depends on OPEC. They can basically do anything they please, and we are having to pay their price.

Estimates we have gathered from our 27-county area, that we like to call the Big Country, show more than 15,000 workers in the oilfield who are directly involved in the oil and gas extraction business. The payroll for those folks totals \$400 million. Spilling over to the rest of the economy, another 62,000 people work in energy-related areas. That flows with the State comptroller's estimates that for every worker in the oilfield, itself, there are 4.3 other jobs created out there supporting him. Those jobs are being dramatically affected by the oil-price crash and the ensuing cutbacks. For the

last 14 months, Abilene has averaged 5.8 percent unemployment. However, in 4 of the last 5 months, we have been above that average. Last month in February, it skyrocketed to 7.7 percent. That is only one-tenth of 1 percent less than the all-time record high of 7.8 percent in June 1982.

The picture does not get any brighter. Last month, Eastman Whipstock laid off 42 workers. The firm puts together sophisticated oilfield survey equipment. There have been other layoffs in the industry, but the overall economic impact has begun to flow over into the rest of our business world.

At this point, I need to interject an explanatory note. I cannot honestly tell you where the line is drawn between the oil-patch-related problems in our economy and those that may have been caused by poor business judgment, shaky financial standing, and the like. But we are having some real problems. More than 100 retail establishments, which were operating during 1985, are not open today in Abilene. They range from the mom-and-pop gift shops, to resale stores, to one of the oldest and largest department stores in Abilene.

Sales tax revenue, one of our best ways to judge just how it is going in the business community, grew 8 to 12 percent statewide last year. It fell 1.3 percent in Abilene. Building permits dropped to a 5-year low, both in volume and in value. Commercial construction was hit hardest in 1985, with its total being only 40 percent of the value that was permitted in 1984.

The picture is not pretty. I am sorry. And thank you.

Mr. STENHOLM. Thank you, Mr. Williamson.

Mr. Combest.

Mr. COMBEST. Thank you, Mr. Chairman.

Dr. Fisher, what would you recommend, should we have an imported oil fee, that the level be set? I presume when you say sliding schedule, you set it at a constant figure and the higher price comes—OK. What would you suggest that figure be?

Dr. FISHER. You try to get down to figure for replacement costs, but they vary tremendously. What you should do is peg a price at a level necessary to make additions to stabilize production as a measure of national security. That is the principal point.

If you look at what the average price has been over the last 3 or 4 years, or certainly since about 1980, that has been sufficient to encourage the level of drilling in the oil patch to raise additions up to the point, roughly, level to the production level. We have almost stabilized production. In the lower 48, we have flat stabilized the production of crude. The level actually increased a little bit after it had been declining 4 or 5 percent a year throughout most of the 1970's. So that arrest of the decline was a very, very substantial one.

I would suggest a price very similar to that, probably in the \$27 range, more or less, and depending on how you figure the windfall profits tax and other kinds of factors in it, is one that is sufficient to give you the volume of oil completions and drilling activities to give you the reserves to stabilize production. And as a national security point, that is what you want to do so you can manage the volume of imports, or keep them in the 30- to 35-percent range.

If you try to attack this in terms of just a plain replacement cost on oil, that range is almost an order of magnitude around the world, from very, very cheap stuff to stuff that is very expensive. Some people would say what does it take to go back in and open up a well that was a plugged stripper, at 2 barrels a day. Well, it may be \$60 or \$80.

But in a reasonable range, something like about \$26 or \$27, in the upper \$20's would be sufficient, I think, in real terms to spur the kind of activity that would give us production compability in the United States.

Mr. COMBEST. Congressman Stenholm mentioned in his opening remarks that this is my first term in Congress. I was in Washington before I was sworn in in December 1984, when the tax reform legislation actually first reared its ugly head. And since that time, I know in my district and in others, there has been a substantial decline in new rigs. Rig count continually went down, even at the end of 2 years, toward the end of the year when normally it is usually highest.

Some of the current problems, obviously, were caused by other factors as well. Do you have any idea—certainly I would understand if you do not—but do you have any idea of what has happened in Texas since, let's say, January 1, 1985, through the end of 1985 in terms of—

Dr. FISHER. In terms of drilling activity?

Mr. COMBEST. Yes, sir.

Dr. FISHER. Well, completions were off about 12—as I recall, about 12 to 13 percent on the oil side what they had been the year before. They actually increased on the order of about 18 percent the year before.

How much of that one attributes to the uncertainty attendant to the proposed revisions of the Tax Code, I guess, is a little difficult to really put in. But I am sure it had a major effect.

Mr. COMBEST. Of course, it is very difficult to know that for certain. Just in talking with people that are in the business, there was real difficulty in getting money when people have no idea of what the rules of the game are going to be. Hopefully, that is a fact which we could put aside and get rid of in terms of—

Dr. FISHER. If I may, we used the Tax Code for many, many years in this country, in the case of oil and gas, for very good legitimate reasons, to pursue a marginal resource; marginal in the sense of compared to the cost or producing this in other parts of the world, and I think to exceedingly good advantage.

If you look at what we are producing today, just in crude oil, it is at least 2½ million barrels a day more than we would have produced if we had stayed at the same production decline that we had in the 1970's. That is very substantial, that arrest in production. A lot of it is using the Tax Code as a positive incentive. And, sure, it is a use of government. There is a government involvement in it, but government involved for a very substantial purpose, and that primarily being national security and the maintenance of production capability domestically.

Mr. COMBEST. Mr. Williamson, were you in Abilene in June 1982?

Mr. WILLIAMSON. No; I was not.

Mr. COMBEST. Do you have any idea of what that 7.8-percent unemployment was attributed to?

Mr. WILLIAMSON. I really do not know. I'm sorry.

Mr. COMBEST. In your business, as business editor of the Abilene Reporter-News, you obviously have opportunity to visit with a lot of people in business.

Mr. WILLIAMSON. Yes, sir.

Mr. COMBEST. What is the basic businessman's attitude in terms of not only the problems that he sees—I mean the businessman other than the producer, or other than supply industry, or something of that sort—what is the basic attitude in that; where does the sympathy come? Does the sympathy come from the fact that his—let's say a drugstore or a flower business—business is down.

How much do they, in your opinion, actually know about the oil business and why we have a problem, or do they just perceive that, "Gee, we've got a problem; we have to get the price up"?

Mr. WILLIAMSON. I think the latter is probably true. They really do not understand. I am sure I do not fully understand what the oil situation really is. If you are not working with it day to day, I think it is pretty complicated and tough to understand.

They can quickly see it in their cash registers. That talks louder than most anything, I believe. They are very cautious right now, the druggist, or dress shop, or whatever. A lot of our businesses here laid off people at the beginning of the year. They were uncertain about the economy at that time. They were telling these people that they may be back on the job in 2 weeks or 2 months, or maybe not at all, because they just did not want to go in too fat into 1986.

To specifically answer your question, I really do not have a good answer. They do not understand exactly how oil relates, and all the interworkings of it. But they understand it when that cash petroleum price goes down; so does that money in their cash register.

Mr. COMBEST. One of the problems, of course, that I think we are confronted with in looking at it from a legislative standpoint, whether it be taxes, or whether it be an imported oil fee, or whatever, is that in the 40-some-odd States that are not producing States, the national economy at this point, apparently on paper, is doing well. A lot of that is being attributed to lower energy prices and the resulting economic good that comes from that. It is going to be fairly difficult for some people to vote for something their constituency is going to see as raising gasoline prices, or raising home heating oil, or doing whatever.

So it is an overall—I think the people that are here understand the problem much better because they see it very directly. That is the message we have got to get through.

I do not know, this is certainly a guess, but I am going to submit, based on what was happening in the Permian Basin in 1982, their high unemployment rates down there at that period of time were a result of some difficulties we were having in the industry; I would not be a bit surprised if we do not look back at some articles that were written about that time in 1982 in the Abilene newspaper, that it was because of some very severe problems in the energy industry at that time.

Mr. WILLIAMSON. Yes, sir; I believe you are correct about the paradox, that 40 or whatever number of States that are not really oil oriented, that it is hard for them to understand what we are going through. And I think a lot of us are having the same problem. It is nice to drive over to the filling station and pay 84 cents a gallon to fill up. But then when you see what it is actually doing to the economy, it hurts.

Mr. COMBEST. Thank you very much.

Mr. STENHOLM. Following up on that, I think we have been in a depression in agriculture in this country for several years now. We have been shielded in this area because of the boomtimes of the energy business. I think that we are now able to fully appreciate what has happened to the agricultural industry in this area, just as in many other areas, particularly the Midwest. We are now seeing it, and it is not a very pleasant sight.

Dr. FISHER, one suggestion was made in Washington to support stripper well production at a fixed price of \$15 per barrel with the same type program for stripper well production that we've got for peanut production.

Would you comment on the feasibility of keeping these wells on line by providing for a fixed price through a quota system?

Dr. FISHER. Mr. Chairman, as long as one makes the assumption that it is in the national interest, national security issue to have x amount of production, then if you can do that at a reasonable price, it is obviously worth doing. That is the only kind of counter one can have as an argument for subsidizing a piece of marginal production when somebody else says, "Well, we can import it for \$10, you know." If you have no concern relative to national security, you do not really care about what kind of vulnerability you may put yourself in in the long haul on this thing, then you just lay back and take it, and get it.

I would argue very much that it is absolutely a critical point; we can control our destiny in this country if we can keep our production within about 65 percent, or that range, of what our demand on oil is. And one of the very critical components of that, of course, would be maintaining stripper production. That is still about 18 percent of total production in the United States. And in some areas half the production comes from strippers. And the maintenance of that, since if you plug it, for all intent and purposes, it is lost and it is lost forever. And that capacity that we lose this year by dropping out the strippers is lost. We still lose it next year because those wells that are making 11 barrels will move into the 10. And that is a dynamic progression as you move into some of those kinds of decline.

Yes; they are worth keeping. They are worth maintaining at a price because if they are lost, they are lost forever. And I make that issue not because you can maintain them at a cost less than what the Saudis are willing to sell you oil for right now, but in a longer term national interest and that is where the other 45 States have to be concerned.

Mr. STENHOLM. Well, it is not just the other 45 States we have a problem with. Consider public perception of the agriculture and energy industries.

Today most polls show that we have more support for agricultural programs in urban America than we have in rural America. I think that is very interesting; 92 percent of my constituents are not farmers, and many suggest to me, sometimes very heatedly, that I spend too much time on agricultural policy.

There is a perception by most of us that there is nothing inherently bad about cheaper gasoline, lower electric bills, or some of the other lower energy costs we are currently experiencing. In the long run, though, we must recognize the inevitability of where we are headed.

Dr. FISHER. We have some remarkable recent history, Mr. Chairman. And I appreciate that it is hard to get that across to the general population. But we went through this wretched cycle of roaring up and crashing down, and that is not something that happened 50 years ago; it happened about 6 or 7 years ago. We have come right through that.

One of the very substantial reasons that we have had low inflation, I think, there are a lot of factors that have played into it, and tax policy has certainly been one; but also the fact that we have had rather stable energy prices during that period of time. That contributes tremendously. We go through this up or down; we will get those kinds of economic dislocations and inflationary things that cost everyone, whether you live in urban areas in the East or whether you live in Abilene. You get it all the way. Those are hard issues to make, but they are ones that simply have to be made, I think.

Mr. STENHOLM. You have stated it very clearly.

Mr. Williamson, do you believe price stability in energy is desirable?

Mr. WILLIAMSON. I think if we had the price stability for the small businessman, he would at least have a better grasp of where things are going. It would help him do a better job of planning and carrying out his business if we had the oil price stability, if it was not so much uncertainty of where the heck it is going to go next. I think it would help the small businessman; yes.

There is a lot of doubt out there. They really do not know what is happening and what is going to happen next. Of course, I guess no one does other than our friends over in Saudi Arabia.

Mr. STENHOLM. Senator Bentsen requested the Joint Economic Committee to study the macroeconomic impact of falling oil prices. The study concluded that the extravagant claims for a dramatic resurgence of economic growth due to falling oil prices are without justification. Real GNP this year will rise less than 1 percentage point due to lower oil and energy prices, and nearly 80 percent of the impact of falling energy prices will be offset by eroding revenues to the domestic energy sector and resulting ripple effects.

And also as a result of what we are now seeing today, announced layoffs in the automobile industry because of the decline of automobile sales, et cetera, and we are seeing this again in agriculture because of the lack of combines needed, tractors needed. You cannot buy it with money you do not have. So there is an offsetting economic impact, wherein a lot of people thought this was really going to be a boon, if we are only going to get 80 percent of the benefit of the bust back into the overall economy.

Do you agree with that assessment Dr. Fisher?

Dr. FISHER. I have read the report. And I thought the analysis seemed quite appropriate; it was quite logical to me. It was pointing out the broader implications of energy use and what that means in the country, and the broader use of the participants. And, particularly, I think it was important in the agricultural side where the number of farmers and ranchers that are able to maintain because they are able to lease the mineral rights of acreage that they hold. And that was a significant point, I think, in that particular analysis that was done for Senator Bentsen.

Mr. STENHOLM. Doug, I believe you said you haven't seen this report.

Mr. WILLIAMSON. I really have not seen it; no.

Mr. STENHOLM. Over the past few years decisions have been made by the Federal Government to cut back research into alternative forms of energy.

Hardin-Simmons University here in Abilene is currently hosting a symposium regarding microbial-enhanced oil recovery. This is an area of research and development which needs to be pursued. It is short-sighted not to have more Government-supported research in the area of energy development.

It just seems to me that we may be making a mistake right now by not putting a little more emphasis on research and development. There are current needs, future needs, and national security implications to consider. Please comment on that.

Dr. FISHER. What you do not invest in, you do not have in the future. It does not matter whether it is in research or something else. If you do not put it up now, you do not have it when it comes down the line.

In the particular case of energy R&D, and particularly in oil and gas, whether public sector R&D or Federal Government, I think is really quite lamentable, the direction we have gone. I think we are missing some opportunities that would have rather substantial pay-offs.

The stabilization of oil production that has occurred in the lower 48 and has almost occurred in Texas has been 80 percent from reserve additions that have come from the ability to get more oil out of the existing reservoirs, old reservoirs. And that is where a lot of the activity is out here. And it is not an idle pastime. We have in Texas alone better than 110 billion barrels of oil in reservoirs, known. We have to work on the process to get it out. Each year, we improve a little bit more. To the extent that we invest in R&D, whether it be microbial recovery or a variety of other things, these are the kinds of things that have substantial payoff down the line. And the target is big. And if you translate it nationally, we are talking about in excess of 400 billion barrels.

So it is not the kind of R&D that you say: "Well, I don't know even if we're successful whether it's going to get us anything." You know if it is successful, you have a major target that it is applied to. It is of very real interest to this country.

Mr. WILLIAMSON. I think the west Texas oilmen right now are more concerned about what is happening today and tomorrow. They have got the blinders on. Next week is something else. Next year and the next decade is way far into the future and have noth-

ing to do with what is happening today. They are looking at the price of west Texas intermediate crude on the New York Mercantile. They are looking at what is coming out of OPEC meetings and whatever the various oil ministers are saying. I think the consumers are looking at the easy-serve price of 84 cents a gallon. And that is all that is being looked at right now.

I think you are absolutely correct that there is no sight into the future at this point. If we do not have some peripheral vision to see what is happening there, something even worse can sneak up on us, I'm afraid.

Mr. STENHOLM. Let's face it; if you are an oil producer or a farmer on the verge of bankruptcy, you could care less about long-range policy for anything. That attitude is understandable in all of us.

The administration wants to stop filling the strategic petroleum reserve, despite current low prices. It would seem to me that it would be a better national policy to buy as much of this cheap foreign oil as possible and place it into our strategic petroleum reserve at current low prices. Yes or no?

Dr. FISHER. Yes; why not? If you can get it cheap, why not do it?

Mr. STENHOLM. The administration policy is that we not buy any foreign oil at this time, in order to meet budgetary considerations. Do you have any comment, Doug?

Mr. WILLIAMSON. Yes; I think there is no question that we need to go ahead and go after the cheap oil. We are starting to feel the Gramm-Rudman pinch already pretty hard.

Mr. STENHOLM. Another one of the suggestions is that the Government buy some of this stripper oil at a little higher price and pump it into the reserve, just to keep marginal production going.

Dr. FISHER. I have real fears that this is not a temporary situation. I wish it were. And I make that point that it is longer term, that it will take 3 or 4 years until such time as enough marginal capacity around the world is knocked out. Most of that is in the United States. A lot of it is right out here within a rock's throw of us when we are talking about stripper wells.

And I make that point, Mr. Chairman, because I am pretty well convinced in my own mind that there is no capability, no entity around that is able to serve as a swing producer, and that has the ability to administer a price. We have always administered the price of oil. If we want one and want a stable replacement cost, it has to be done because of this wide range of intrinsic value of the oil around the world. If we want that, we have to do it. And I think there no longer exists that capability. I think the Saudis have lost it. They can come and sell oil at \$10 a barrel. And if they sell three or four times as much of it, if they increase their market share that much, they have a better revenue situation than they do if they are producing 2 million barrels a day and trying to protect the price for everyone else. They have got very little to lose by what they are doing. The people that have the most to lose, though, is the United States.

Mr. STENHOLM. Thank you very much for a very interesting and stimulating testimony and response to our questions. We appreciate very much you taking time to be here today.

We call the next panel. Mr. Glen Michel, Mr. John Chalmers, and Dr. Earl Harrison.

The first witness will be Mr. Glen Michel for the National Stripper Well Association. Glen, welcome.

**TESTIMONY OF GLEN MICHEL, EXECUTIVE VICE PRESIDENT,
NATIONAL STRIPPER WELL ASSOCIATION, ABILENE, TX**

Mr. MICHEL. Thank you, Mr. Chairman. Welcome back to Abilene. We are glad to have you.

Mr. Chairman, my remarks might appear to be national in scope since I do represent a national organization. But I think in this case that what affects the Nation will also apply to our local scene since we do operate a lot of stripper wells in this immediate area.

I think, first of all, that I would like to give the subcommittee some facts to see the magnitude of this problem we are talking about because I think it affects 8,000 to 10,000 small, independent oil business people. And I think if we look at the total inventory or producing wells in the lower 48 States, there are 73 percent stripper wells. And these wells produce 15 percent of the Nation's total production each day. The wells average slightly less than 3 barrels of oil per day, and there are 452,543 wells of this type.

In 1984, they produced—these are all 1984 figures, for the committee's information because we have not compiled our 1985 figures yet. These wells produced 463,458,703 barrels of oil for the Nation in 1984. And most of the wells are operated by small, independent oil operators.

I think just to know that our Nation is in this shape, knowing that 73 percent of the Nation's wells in the lower 48 are stripper wells should give us some cause for alarm as to the energy base for this Nation.

Now that we have had this precipitous drop in crude prices, we could lose as many as half of these wells by either plugging or temporary abandonment. And we are aware in the stripper well organization that we have 4½ billion barrels of reserves under this type well, and we believe we can recover 2½ billion barrels of that oil by primary, and 2 billion barrels by secondary recovery methods. And I am primarily in secondary, speaking of water-flood operations.

How much additional oil would be recovered by tertiary methods, namely micellar and polymer projects at this juncture, we do not know. We have no way of knowing of new techniques that may come onstream for us in the future.

I do not think that any of this recovery will be possible—well, at least probably not half of it—if we force our small, independent, entrepreneur-type, business oil people out of business. And the main thing that will run them out of business is, of course, the price of oil.

But I think we had better look further down the line than that. The plugging and abandonment of stripper wells, that is really only the—just the first shock wave.

There are wells, many wells throughout the Nation and particularly in 7(b), 9, 7(c) in Texas, district 10 in the Panhandle, that do not fall in the stripper well category. They may make 12, 14, 15

barrels a day. They may be 5,000 to 6,000 feet deep, with a high water content. And I am sure that many of these wells are quickly, if not already, reaching their economic limit.

We, as a stripper well association, have made a preliminary survey of lifting cost for stripper production. This survey covered wells in Texas, Oklahoma, Illinois, Louisiana, and I forgot to add Kansas, which is mainly a stripper well State.

Our findings reveal that tertiary production had a per barrel lifting cost in excess of \$17 a barrel and, in many cases, up to \$22 and \$25 a barrel. Secondary recovery projects had an average of \$14 per barrel lifting cost. And primary production indicated lifting costs could go as low as \$6 to \$8 per barrel, particularly where the water content was low and, in most cases, operated by very small firms with little overhead costs.

In our own local Abilene area, by personal survey locally, it was indicated that lifting costs for our stripper well crude here ran from \$13.32 to \$13.63 per barrel. And this is not considering administrative overhead costs figured in, which would run that cost close to \$14.50 per barrel lifting cost.

When we averaged out all of these costs, the national average for stripper production amounted to right at \$14.50 a barrel lifting cost. I don't think it takes too much calculation to readily see that an awful lot of the stripper well inventory has already reached its economic barrier, and that something must be done immediately.

My office has had 50 to 75 calls from various agencies nationwide. These calls were from the Department of Interior, the Department of Defense, Texas Governor's Office, and the list is too numerous to mention. I would be happy to discuss these calls with this subcommittee immediately following this testimony if the chairman so desires.

I think it is well to point out here, we talk about a \$9.75 cost per barrel or crude or we talk about a \$10.31 barrel cost. Our local price is \$13.75 a barrel, less \$1 transportation charge, which nets the producer \$12.75 before ad valorem and other taxes come out of that barrel of crude.

To get back to the abandonment of wells, let us assume that we are forced to plug almost a quarter of our Nation's stripper well inventory. That would be in the neighborhood of some hundred thousand wells. And at three barrels a day, we could lose as much as 300,000 barrels of production each day. I think Dr. Fisher's figure was around 400,000, and I am not in disagreement. It could even go higher than that.

If we take that 300,000 barrels that we produce and put it in the scenario that we lose each day for 365 days a year, and we are forced to purchase those barrels from some foreign source at \$12 to \$15 a barrel, I don't think it takes much imagination to see what it is going to do to the balance of payments. But I think the worst part of the whole scenario is this; we will be leaving millions of barrels of reserves in the ground that probably never be recovered because the economics for redrilling these reservoirs, such as the type reservoirs they are, will mandate that we have oil in the \$50 to \$60 per barrel range before the economics will permit us to re-drill.

Mr. Chairman, now this depends on whether or not the depth of that well—whether we are going back to primary or whether we are going into a secondary project, whether a five-spot or a peripheral flood, or whether we are going into a tertiary project. It could run as high as \$70 to \$80 a barrel in some cases.

These abandonments that I have referred to have a real domino effect on the local economy as well as the Nation's economy, particularly where your primary economic base is oil.

Not only will we lose our small independent oil operators, but we lose jobs at an alarming rate. I know of many operators already, I have talked to them personally, who have had to cut salaries for their people 10 to 15 percent and as much as probably 10 to 20 percent of their people are already gone from the payroll, trying to cut costs, trying to cut lifting costs, trying to do everything they can to keep that production on stream.

This filters right on down to our drilling companies, our well-servicing companies, cementing services, logging companies, supply stores; goes right on through our merchants, goes right on down the line.

Texas has, out of that 452,000 nationwide stripper well inventory, 126,202 of those wells. And had it not been for the recent actions of the Texas Railroad Commission, we would have already started to plug 25 percent of those wells because they are no longer economic. I think that was one of the finest things that the Railroad Commission did. They extended our plugging period from 90 days to 1 year, and gave us no bonding provisions in that new rule, amendment to the rule.

As it is, I think many wells will have to be temporarily abandoned until we can determine what the price of crude oil is going to do. I know some operators already with 8 or 10 well leases are now having to pump one well to maintain the lease because many of our leases—most of our leases, maybe all of them, John, have a 30- or 60-day clause. At the time of cessation of production, we must. Without reworking the lease, without pumping the lease, it reverts to the landowner.

Here is a case where we may have to go to our royalty owner, if we have been a good tenant, and plead with him to extend the time period in which we have to return the lease; because not only do we lose, but he loses also, and we lose those reserves as well as he does. I think this is a thing that the royalty owner and the land owner and the producer/operator will have to work among themselves. In many cases, of course we have a multiplicity of royalty owners and it is going to be extremely difficult. But I think that effort will have to be made.

I think in Texas we are going to be probably hurt worst than a lot of States because oil has been our main tax base. Particularly in your own district, Mr. Chairman, in the 17th, and I suspect in the 19th, too, Mr. Combest. Our tax base is primarily oil and agriculture. So I know that our schools, our cities, our county governments, every facet of our economy is going to be hurt from this lowering of the price, the losing of the ability to tax our—you know, we have a double tax. We have one on our equipment, we have one on the minerals. So we are going to lose a little of each if

we are forced to plug and abandon these wells, or even temporary abandonment is going to be hard on the operator.

I think I would like to comment on one last thing, Mr. Chairman, and that is that I have been in the industry—I should not tell you how long because it gives away my age. And I have experienced about three of these recession periods. But as far as I am concerned, this probably has been the worst one because of the precipitous drop that we have experienced in a 2- to 3-month period.

I think since November the 1st until now, we have had a 66-percent drop in our crude prices. I think that what makes this one really so bad is that our producer has been caught with an extremely heavy debt load. Frankly, gentlemen, I think some of them are just not going to survive. I hate to say that, but that is probably just a fact of life. I sure hate to see it happen.

Not only will some of our small producers and small business people not survive, but it is going to cause a very severe strain on our financial institutions and, in fact, it already has.

Mr. Chairman, this concludes my remarks. And I would like to get back to you on some of these other points if time permits.

Thank you very much for letting me appear.

[Stripper well survey follows:]

NSWA

NATIONAL STRIPPER WELL ASSOCIATION
 Box 3373
 Abilene, Texas 79604

QUICK FACTS

NATIONAL STRIPPER WELL ASSOCIATION

All references are to stripper oil wells, defined as those producing barrels or less daily.

Producing stripper oil states	28
Total production, 1984	463,458,703
Production, percent of U.S. total	15%
Value of production (est.)*	\$12.0 billion
Paid directly to farmers, landowners, as royalty (est)*	\$1.9 billion
Total producing wells	452,543
Percent of U.S. total all wells	73%
Avg. daily production per well	2.80 bbl.
Productive acres	10,399,270
Recoverable reserves	4.5 billion bbl.
By primary recovery	2.5 billion bbl.
By secondary recovery	2.0 billion bbl.
Wells abandoned, 1984	14,170
Avg. abandonments, last 5 years	9,691

Based on average 1984 crude value

Information based on National
 Stripper Well Survey for January
 1984 or calculated by NSWA



NATIONAL STRIPPER WELL SURVEY

JANUARY 1, 1985

A JOINT PROJECT OF THE
INTERSTATE OIL COMPACT COMMISSION
AND THE
NATIONAL STRIPPER WELL ASSOCIATION

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INTRODUCTION

You are holding in your hand the only survey of stripper wells which is produced in the entire world. This is remarkable because the United States is the only nation in the world which has marginal or stripper wells. A marginal well -- the subject of this survey -- is a well which produces fewer than 10 barrels a day. On December 31, 1984, there were in the United States 452,543 wells which fell into that category. As you will learn if you go through this survey, these wells produced 463,459,000 barrels of oil last year. On the average, each well perked (or pumped) less than three barrels a day. You will also learn that 14,170 such wells were abandoned during the year. The abandonments are a loss in the United States because each of these wells is capable of producing a small amount of oil, but the amount became too small to pay the taxes, royalties, and operating expenses to keep the well open. Once a well producing less than the average of 2.8 barrels is abandoned no conceivable scenario can be written for ever redrilling that well and recapturing the lost resource.

A combination of factors enter into the fact that this country is the only nation that produces its marginal reserves. Sound regulation, good conservation, private ownership of minerals, and an aggressive industry are all factors. The average oil well in the United States produces 14 barrels of oil per day. The average oil well outside the United States produces 290 barrels.

As long as we are a nation that relies on liquid fuels -- gasoline, heating oil, jet fuels -- we will have a need for more crude oil than can be found and produced in the United States. This aggravates the problem of balance of payments. The true value of a stripper well is that every barrel of oil it produces is a barrel the United States does not have to purchase from a foreign government.

W. TIMOTHY DOWD
Executive Director
Interstate Oil Compact Commission

October, 1985

FOREWORD

Stripper oil operations in recent years have clearly demonstrated that increased incentives result in increased oil production.

This was again true in 1984 when the nation's stripper oil wells -- wells that average 10 barrels or less per day -- registered an increase of more than 1.4 million barrels in a year's time. That followed increases of more than 20 million barrels in 1983, more than 15 million barrels in 1982 and a gain of more than 25 million in 1981.

This contrasts sharply with the pre-embargo trend of losses averaging 15 million barrels a year.

The National Stripper Well Survey, published annually for more than 40 years, is the result of joint efforts by the Interstate Oil Compact Commission and the National Stripper Well Association. Its purpose is to provide national and state-by-state data on stripper well operations.

This current report shows that there were 452,543 stripper wells in operation as of January 1, 1985, and that during the 1984 calendar year 463,458,703 barrels of stripper oil were produced. By comparison, there were 441,501 stripper wells as of January 1, 1984 and during 1983 calendar year they produced 462,013,486 barrels of crude oil. Thus, there was a one-year increase of 11,042 wells and an increase in production of 1,445,217 barrels.

The nation still has a long way to go to reach energy independence, but the record of stripper oil operators illustrates the right direction for a continuing move in that direction -- adequate incentives to domestic oil producers.

It is hoped that Congress will keep this in mind during its everlasting search for more tax revenues and that it will conclude it is in the nation's interest to increase domestic oil production rather than increasing oil taxes.

From 1972 to 1980 abandonments decreased from 13,483 down to 6,614. Increased price of crude oil, no doubt, extended the life of all stripper wells.

In 1981, the number of stripper wells increased about 600 nationwide to 7,215 and in 1984 to 14,170, an increase of 15. This, no doubt, can again be attributed to price decreases and any change in stripper well tax provisions will cause an even greater increase in well abandonments. All of this points out the fact that the stripper well industry needs improved recovery techniques.

What all this means is that higher prices extend the life of these wells and that this permits America to have the beneficial use of more of its natural resources. Every barrel of oil resulting from a longer life for stripper wells means the United States will reduce its dependence on overseas imports by a similar amount. Too, it means greater revenues in the communities and states where stripper oil production is increasing. And it means more jobs.

The National Stripper Well Association, organized in 1934, works in the interest of stripper well operators, but within the boundaries of what is best in the national interest and what will help meet our energy needs.

It is necessary to detail the methodology and parameters used in this study. The data presented represent a compilation of information from various contributors in oil-producing states with stripper oil production. Some states, such as Alaska and Florida, have no wells in this classification.

In the state-by-state data in this report, the production in barrels from stripper wells represents the total oil produced from all stripper wells during the year. The acres shown are those attributed to these wells, and include acreage within stripper well fields which is no longer productive.

The abandonments are the number of producing oil wells that have been abandoned during the year. Some of these may not have been classified as stripper wells, but practically all of them are assumed to be those which could no longer be economically operated under prevailing conditions.

Total production from each state in 1984 was obtained from state agency records or from other sources.

Primary reserves are the estimated additional oil to be recovered by primary means from stripper wells and stripper well fields included in this review. Secondary reserves are those estimated to be recoverable from the listed stripper wells and stripper well fields by secondary recovery. These include: (a) amounts to be recovered from the developed areas of current secondary recovery operations; (b) secondary recovery oil estimated to be produced by expanding areal extent of current operations; and, (c) secondary recovery oil estimated to be produced from fields where secondary recovery operations are not under way, but where conditions are considered to be favorable for successful development of secondary recovery projects.

The estimated secondary recovery production from stripper wells during 1984 and the percent of total stripper well production coming from secondary recovery projects were furnished for 16 states. This information is presented on the following page, together with a table showing stripper well production year-by-year for the past 10 years.

R. HARLAN KRUMME

PRESIDENT

NATIONAL STRIPPER WELL ASSOCIATION

State	Estimated Secondary Oil Produced from Stripper Wells (M Bbls.)	Percent of Total Stripper Production from Secondary
Alabama	6	03.49
Arkansas	1,180	20.87
Colorado	500	15.02
Indiana	2,084	47.35
Kansas	20,663	42.47
Kentucky	3,441	54.62
Missouri	134	49.47
Nebraska	1,041	35.00
New Mexico	1,915	19.88
New York	579	85.15
Ohio	94	00.88
Oklahoma	51,665	54.94
Pennsylvania	1,314	30.98
South Dakota	41	49.94
Tennessee	65	12.75
West Virginia	660	20.18

STRIPPER WELL DATA - PAST 10 YEARS - UNITED STATES

Year	No. Wells	Production (M Bbls.)	Abandon- ments	Avg. Daily Prod. per Well
1975	367,872	394,163	13,478	2.93
1976	365,733	392,191	9,916	2.93
1977	368,930	392,532	9,000	2.91
1978	374,635	391,633	8,380	2.86
1979	386,310	394,405	7,668	2.79
1980	395,176	401,095	6,614	2.77
1981	409,539	426,502	7,215	2.85
1982	416,493	441,951	9,426	2.90
1983	441,501	462,013	11,032	2.87
1984	452,543	463,459	14,170	2.80

NATIONAL STRIPPER WELL SURVEY AS OF JANUARY 1, 1985

STATE	NUMBER OF STRIPPER WELLS	PRODUCTION FROM STRIPPER WELLS (Bbls.)	ABANDON- MENTS	AVERAGE DAILY PRODUCTION PER WELL	ACRES
ALABAMA	98	171,757	3	4.79	4,461
ARIZONA	14	29,034	1	5.67	760
ARKANSAS	4,738	5,653,341	62	3.26	135,220
CALIFORNIA	26,650	57,124,547	1,126	5.86	254,840
COLORADO	1,690*	3,329,600*	36*	5.38	67,400
ILLINOIS	29,942	25,983,900	629	2.37	678,060
INDIANA	6,134	4,401,175	366	1.96	351,715
KANSAS	45,749	48,664,820	1,505	2.91	1,401,400
KENTUCKY	16,433	6,630,184	393	1.10	65,732
LOUISIANA	16,500	9,844,000	852	1.63	495,000
MICHIGAN	3,500*	3,228,120*	107*	2.52	105,000
MISSISSIPPI	837	1,330,150	96*	4.34	91,840
MISSOURI	548	270,895	#	1.35	5,300
MONTANA	3,085	2,577,082	430	2.28	22,400
NEBRASKA	1,707	2,974,420	36	4.76	67,840
NEW MEXICO	14,749	15,016,044	644	2.78	645,780
NEW YORK	4,532	679,909	140	0.41	217,200
NORTH DAKOTA	1,016	1,755,663	12	4.72	112,680
OHIO	25,129	10,689,770	354	1.16	511,762
OKLAHOMA	82,431	94,045,552	1,491	3.12	1,634,900
PENNSYLVANIA	19,540	4,241,673	848	0.59	97,700
SOUTH DAKOTA	30	82,100	4	7.48	4,630
TENNESSEE	689	510,312	0	2.02	10,330
TEXAS	126,202	152,719,767	4,931	3.31	2,938,640
UTAH	348	1,088,805	22	8.55	25,880
VIRGINIA	32	27,239	3	2.33	1,280
WEST VIRGINIA	15,200	3,270,000	79	0.59	250,800
WYOMING	5,020	7,118,844	#	3.87	200,800
TOTALS	452,543	463,458,703	14,170	2.80	10,399,270

* Estimated.

Not available.

NATIONAL STRIPPER WELL SURVEY AS OF JANUARY 1, 1985

STATE	TOTAL 1984 PRODUCTION (M Bbls.)	STRIPPER WELL RESERVES		
		Primary	Secondary	Total
		-----Thousands of Barrels-----		
ALABAMA	8,486	440	20	460
ARIZONA	215	125	0	125
ARKANSAS	17,868	143,220	28,130	171,350
CALIFORNIA	412,400	207,500	72,900	280,400
COLORADO	29,821	13,600	6,860	20,460
ILLINOIS	28,873	57,225	64,550	121,775
INDIANA	5,360	21,075	17,275	38,350
KANSAS	75,723	191,450	126,850	318,300
KENTUCKY	7,788	22,322	17,207	39,529
LOUISIANA	151,033	71,325	68,500	139,825
MICHIGAN	30,554	22,250	32,000	54,250
MISSISSIPPI	33,116	15,810	2,790	18,600
MISSOURI	271	0	148	148
MONTANA	27,728	30,235	2,275	32,510
NEBRASKA	5,514	25,858	3,709	29,567
NEW MEXICO	75,531	83,650	35,850	119,500
NEW YORK	952	912	7,991	8,903
NORTH DAKOTA	52,654	35,325	27,775	63,100
OHIO	5,271	88,064	292	88,356
OKLAHOMA	156,512	281,100	325,630	606,730
PENNSYLVANIA	4,824	19,952	37,906	57,858
SOUTH DAKOTA	1,333	150	300	450
TENNESSEE	937	970	155	1,125
TEXAS	845,502	1,040,140	1,040,000	2,080,140
UTAH	38,054	7,885	6,195	14,080
VIRGINIA	33	78	0	78
WEST VIRGINIA	3,303	17,664	26,496	44,160
WYOMING	127,763	95,480	75,020	170,500
TOTALS	2,157,419	2,493,805	2,026,824	4,520,629

* Estimated.

Not available.

COMPARATIVE NUMBER OF STRIPPER WELLS AND STRIPPER WELL PRODUCTION

STATE	1981		1982	
	NUMBER OF STRIPPER WELLS	PRODUCTION FROM STRIPPER WELLS (Bbls.)	NUMBER OF STRIPPER WELLS	PRODUCTION FROM STRIPPER WELLS (Bbls.)
ALABAMA	73	121,880	92	157,725
ARIZONA	12	22,561	14	23,944
ARKANSAS	5,847	5,464,994	5,167	5,131,933
CALIFORNIA	26,566	54,803,777	26,354	55,419,356
COLORADO	1,255	2,158,655	1,354	2,203,676
ILLINOIS	25,472	22,238,369	26,813	23,989,100
INDIANA	5,874	4,781,240	5,353	4,567,883
KANSAS	42,924	45,010,362	44,521	47,629,052
KENTUCKY	14,130*	4,479,210	14,275*	5,143,571*
LOUISIANA	15,950	9,011,510	12,010	9,171,973
MICHIGAN	3,057	2,448,521	3,361	2,820,134
MISSISSIPPI	2,138	3,804,738	1,923	2,236,532
MISSOURI	440	226,207	530	52,450
MONTANA	2,058	2,747,952	2,243	2,880,991
NEBRASKA	1,414	2,510,329	1,585	2,878,602
NEVADA	-	-	-	-
NEW MEXICO	13,226	13,462,763	13,882	14,207,219
NEW YORK	5,345	849,000	5,259	719,000
NORTH DAKOTA	836	1,386,140	959	1,492,476
OHIO	21,982	9,485,947	22,966	10,199,361
OKLAHOMA	69,781	83,248,733	73,328	94,236,983
PENNSYLVANIA	25,285	3,605,976	23,438	3,717,935
SOUTH DAKOTA	23	39,340	33	55,444
TENNESSEE	398*	290,540*	#	#
TEXAS	107,596	145,939,797	111,671	143,928,747
UTAH	196	376,596	#	#
VIRGINIA	12	13,244	20	49,424
WEST VIRGINIA	14,300	2,607,133	14,550	2,683,000
WYOMING	3,349	5,366,854	4,792	6,354,517
TOTALS	409,539	426,502,368	416,493	441,951,028

* Estimated.

COMPARATIVE NUMBER OF STRIPPER WELLS AND STRIPPER WELL PRODUCTION

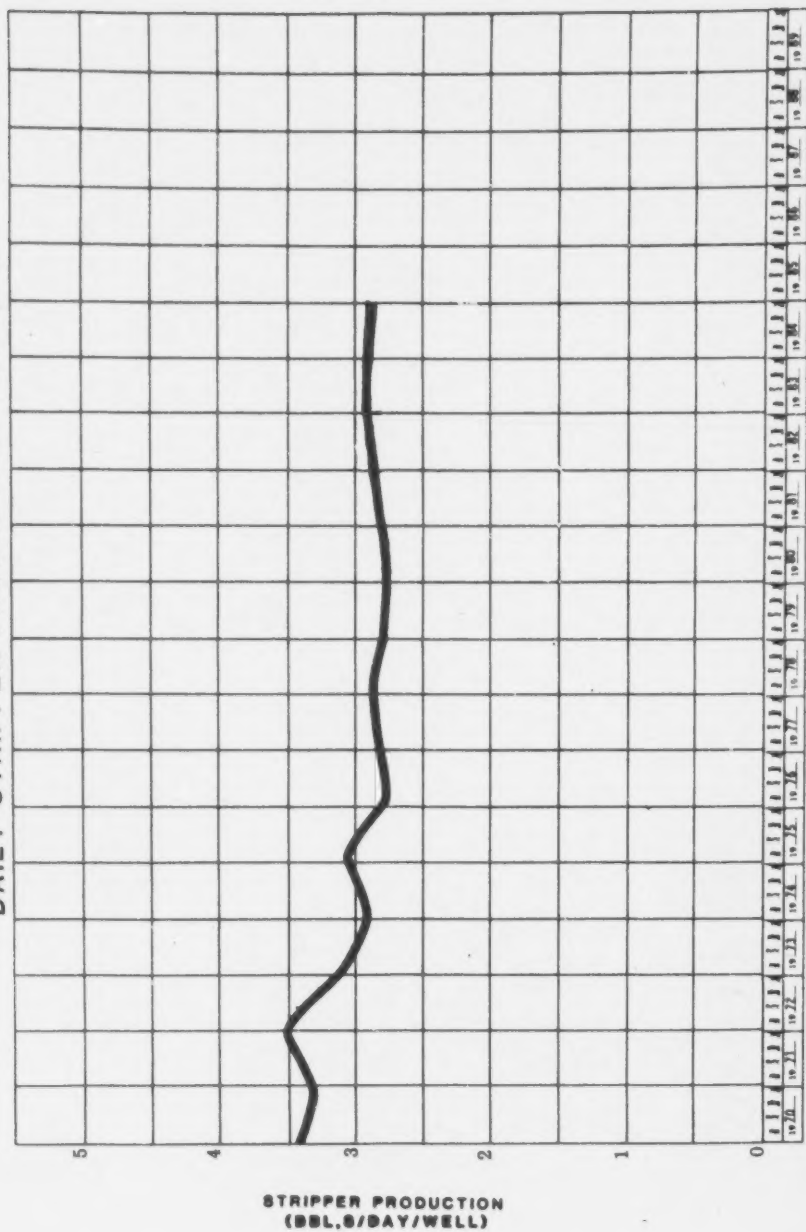
STATE	1983		1984	
	NUMBER OF STRIPPER WELLS	PRODUCTION FROM STRIPPER WELLS (Bbls.)	NUMBER OF STRIPPER WELLS	PRODUCTION FROM STRIPPER WELLS (Bbls.)
ALABAMA	95	172,533	98	171,757
ARIZONA	17	25,626	14	29,034
ARKANSAS	7,218	7,117,852	4,738	5,653,341
CALIFORNIA	26,358	55,993,281	26,650	57,124,547
COLORADO	1,861	3,629,755	1,690*	3,329,600*
ILLINOIS	28,566	25,889,500	29,942	25,983,900
INDIANA	5,854	4,336,384	6,134	4,401,175
KANSAS	47,592	48,267,447	45,749	48,664,820
KENTUCKY	17,000*	5,521,856*	16,433	6,630,184
LOUISIANA	16,500	9,000,000	16,500	9,844,000
MICHIGAN	3,367	3,144,938	3,500*	3,228,120*
MISSISSIPPI	837	1,286,247	837	1,330,150
MISSOURI	548	270,845	548	270,895
MONTANA	2,673	3,103,757	3,085	2,577,082
NEBRASKA	1,672	3,417,977	1,707	2,974,420
NEW MEXICO	14,280	14,722,251	14,749	15,016,044
NEW YORK	4,228	774,283	4,532	679,909
NORTH DAKOTA	922	1,537,331	1,016	1,755,663
OHIO	24,263	10,479,750	25,129	10,689,770
OKLAHOMA	77,729	94,430,484	82,431	94,045,552
PENNSYLVANIA	21,831	3,950,519	19,540	4,241,673
SOUTH DAKOTA	33	43,915	30	82,100
TENNESSEE	716	583,658	689	510,312
TEXAS	117,178	153,688,511	126,202	152,719,767
UTAH	217	542,682	348	1,088,805
VIRGINIA	26	21,571	32	27,239
WEST VIRGINIA	14,900	3,116,500	15,200	3,270,000
WYOMING	5,020	6,944,013	5,020	7,118,844
TOTALS	441,501	462,013,486	452,543	463,458,703

* Estimated.

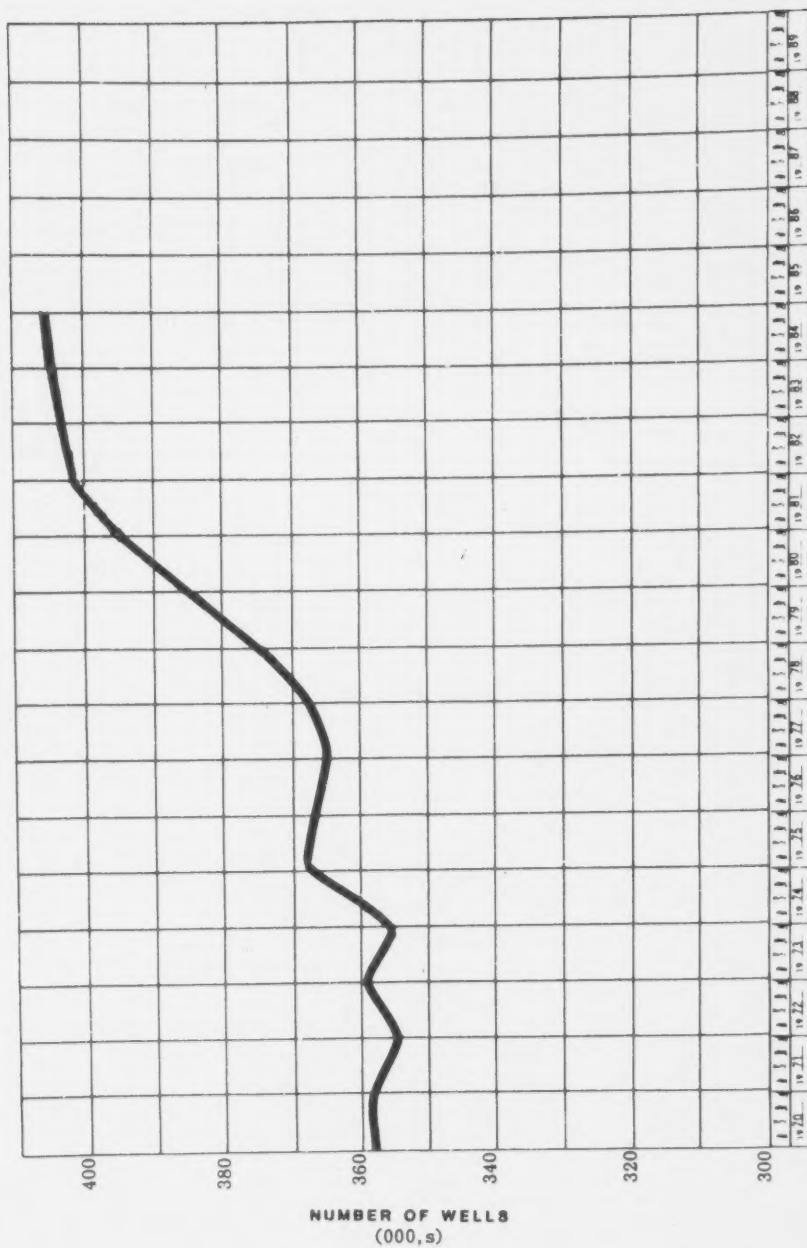
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TOTAL U.S. AVERAGE

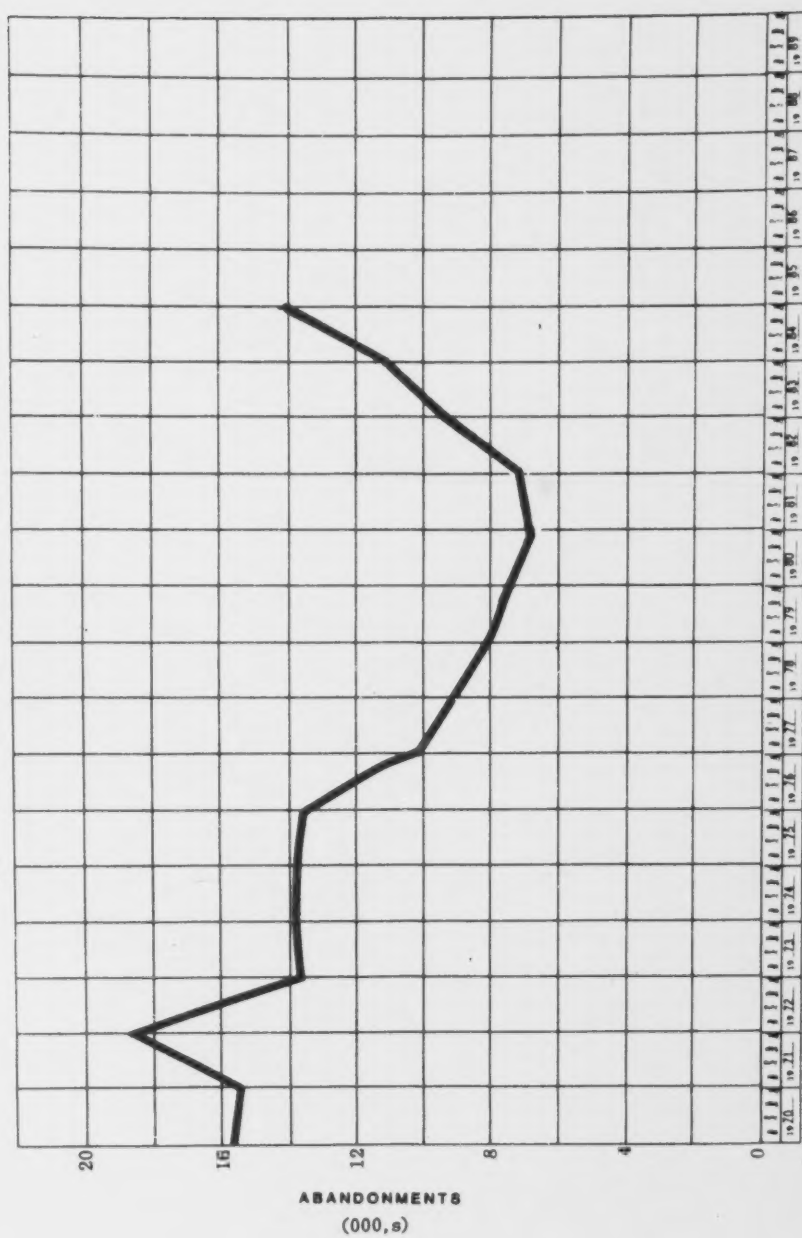
DAILY STRIPPER PRODUCTION PER WELL



NUMBER OF U.S. STRIPPER WELLS



TOTAL U.S. ANNUAL NUMBER
OF STRIPPER WELL ABANDONMENTS



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American Petroleum Institute
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North Texas Oil and Gas Association
Ohio Oil and Gas Association
Oklahoma Independent Petroleum Association
Panhandle Producers and Royalty Owners Association
Pennsylvania Grade Crude Oil Association
Pennsylvania Oil, Gas and Minerals Association
Permian Basin Petroleum Association
Rocky Mountain Oil and Gas Association
Texas Independent Producers and Royalty Owners Association
West Central Texas Oil and Gas Association

Mr. STENHOLM. Thank you.

Next we will hear from Mr. John Chalmers, president and chairman of the board, Chalmers Exploration Co., Abilene, TX. Welcome, John.

TESTIMONY OF JOHN H. CHALMERS, PRESIDENT AND CHAIRMAN OF THE BOARD, CHALMERS EXPLORATION CO., ABILENE, TX

Mr. CHALMERS. Thank you, Mr. Chairman.

First, I want to express Dan Fergus' regrets, president of West Texas Oil & Gas Association, that he had to be in court and could not be here today. And he has asked me to represent West Central Texas Oil & Gas Association as well as myself.

My name is John Chalmers. I am the president of Chalmers Exploration Co., Chalmers Dozer Co., Chalmers Oil Co., Chalmers Rig Service, and Chalmers Well Services. I am actively engaged in exploration for new pools of oil, and I operate or have an interest in over 500 oil and gas wells. I have approximately 50 employees.

I am a graduate geologist from Oklahoma University. I am a grandfather, with five grandchildren. I am a taxpayer. I am active in civic and charitable institutions and local and State organizations. I am a World War II Veteran of Foreign Wars. And I am telling you these things because I consider myself a solid citizen who is vitally concerned about the energy crisis that the United States is rapidly approaching.

For many years, I have drilled approximately 50 exploratory prospects per year. In order to accomplish this, it has been necessary for me to conduct geological investigations, acquire prospective leases, drill and produce where successful, and operate productive wells. Since the exploration costs to find new pools of oil are highly speculative, it has been necessary to furnish potential speculative risk capital investors with incentives to raise sums large enough to conduct the type of exploration programs that I conduct.

It is absolutely necessary that something be done immediately on tax reform. Investors are reluctant to invest when they do not know what type or if any type of tax reform will affect their investment. Two vital components of whether or not I am to stay in business depends on maintaining current marginal and/or stripper producing wells and raising sufficient capital to keep a viable exploration program in operation. I am going to discuss both of these today and make some suggestions on how both can be kept.

Most independent operators in the United States have very similar problems to what I have. First, I want to talk about maintaining stripper and marginal producing wells. I firmly believe that we can keep these in operation today.

The current price of crude oil is \$13 per barrel. When I started off writing this, it was \$14½ or \$15, but we are down to \$13—90 days ago, this price was \$28.50 per barrel. At this price, approximately 50 percent of the stripper leases, that is approximately 452,000 wells in the United States, have a negative cash-flow. There are probably an additional 50,000 marginal wells that have a negative cash-flow. If these wells are plugged and abandoned, then our country will lose approximately 3 billion barrels of reserve. Thousands upon thousands of jobs will be lost. The ripple effect of

the lost jobs will be severe in most of the oil-producing States and areas of our Nation. School taxes, income taxes, State and Federal revenue taxes will present severe hardships.

Current oil operators, petroleum engineering companies, exploration companies, and service companies in this area have been terminating employees for the last 60 days, along with reductions in salaries. This situation will become considerably worse in the next 30 to 60 days as the price of oil continues to drop. In order to stop the downward trend in terminating service companies and oil company employees, it will be necessary to keep all of the producing wells actively producing, as well as to increase the 1,100 active rigs to approximately 3,000 rigs. And we will talk about this a little more in the future.

Most independent producers across the Nation are strongly independent and prefer a clean, free, enterprise system. However, it appears that in order to maintain a per barrel price of oil that will ensure continuation of production, we need Federal help. In order to impose the smallest possible tax burden upon the taxpayers of this country, it is desirable that some system be inaugurated that will return to the Federal Government any aid or subsidy as quickly as possible. In order to do this, I suggest the following:

One, marginal and/or stripper wells receive a subsidy that is the difference between the current price of oil and the fixed price—\$22 dollars per barrel has been suggested. This produced oil to be placed in a strategic petroleum reserve. This oil can be sold at some time in the future at the discretion of the Government. In this manner, this subsidy could actually return a profit to the Government at some future date. This subsidy would be terminated when oil prices come back to \$22 per barrel. In this manner, marginal and stripper wells will be produced and the oil will not be lost. Thousands of jobs will be maintained by company employees, as well as service companies and materials connected with these wells.

The second method that would help do this: If all income derived from the sale of marginal and/or stripper wells with a negative cash-flow could be retained by working interests, it is felt that a great number of wells would be kept producing.

I should add a sentence there that would say we could use 1985 as evidence of a negative cash-flow.

Next item. If all intangible costs connected with maintaining marginal and/or stripper wells were doubled for tax purposes, then a substantial amount of these wells could be kept producing at a negative flow.

Now let us talk about exploration for new pools, and how we can keep finding new oils, and how we can put back together another 1,800 or 1,900 rigs.

At the current time, we produce approximately 9.5 million barrels of oil per day, including Alaskan oil. This is approximately 65 percent of our daily needs; 35 percent of our oil is imported; 55 million barrels per day is either imported in the form of crude oil or refined products. Venezuela produces a combination of refined products and crude oil totaling 600,000 barrels per day. Canada produces a combination of refined products and crude oil totaling

770,000 barrels per day. Mexico produces a combination of refined products and crude oil totaling 815,000 barrels per day.

At the present time, we have less than 1,100 rigs running in the continental United States. However, it will take 3,000 rigs running daily to maintain the daily production of 9.5 million barrels per day that we now produce. If this condition continues, we will need to import approximately 15 percent more oil every year due to the decline in our daily production. In 3 years, we will be importing approximately 65 percent of our oil and our refined products. Approximately one-half of this 65 percent will have to come from OPEC nations, as Mexico, Venezuela, and Canada cannot fill the increased need as daily production declines. What a predicament we are getting ourselves into. Here comes 1973 all over again.

In order to keep 3,000 rigs per day active, it is suggested that we do one of the following. And, fellows, I raise money to get these things drilled. I am the man who contacts people to invest in a speculative venture.

One, all money invested in drilling and/or completion of a wildcat prospect will be given tax credit for twice the money spent. Wildcat wells can easily be delineated from currently producing horizons. This will be a strong incentive for speculative investors, and I think it will truly work.

Two, oil development wells, along with newly enhanced projects will be granted $1\frac{1}{2}$ times intangible costs. This will stimulate development wells and secondary and tertiary projects, as well as keep our stripper and marginal wells producing. In order for companies to invest in development and properly maintain current wells, along with participation in exploratory projects, and to keep current employees on the program, it is suggested that the following be considered: Repeal the windfall profit tax. Repeal incremental pricing. Repeal the Fuel Use Act. Repeal all preferential tax items for a minimum tax. Restore depletion to a full $27\frac{1}{2}$ percent. Open interstate pipelines to equal access, and encourage States to open intrastate pipelines to transportation at reasonable and just rates.

An active 2,500 to 3,000 rigs will maintain our daily production, provide thousands of jobs, keep service companies fully manned, and provide some risk capital for continuing prospecting. If proper incentives are offered for speculative investors, the rigs can be kept busy, and marginal or stripper wells will be kept operating.

I have been raising money to drill wildcat prospects for over 30 years. It is my opinion that risk capital is available for this highly speculative industry provided the incentives are available. If proper action is not taken by Congress with favorable taxes to keep the industry drilling and producing wells, then this Nation will be at the mercy of foreign countries within 3 to 4 years. It is my belief that nations to the north and south of us will take advantage of our vulnerability when our domestic oil is reduced to less than 50 percent of our daily needs.

Very likely, our domestic needs by 1990 will be in the neighborhood of 18 million barrels per day, and our production will be approximately 7 million barrels per day. When this condition exists, the security of the United States is in great jeopardy. Now is the

time for an immediate energy policy that will stimulate drilling and keep all these producing wells active.

I thank you for allowing me to testify before your subcommittee.

Mr. STENHOLM. Thank you, John.

Next we will hear from Dr. Earl Harrison of Acme Production Co., Abilene.

**TESTIMONY OF DR. EARL HARRISON, ACME PRODUCTION CO.,
ABILENE, TX**

Dr. HARRISON. Thank you very much, Mr. Congressman. Thank you for your time and consideration.

My situation is much like Mr. Chalmers', although I am not in the same category John is. I am a small independent oil operator. Being a geologist, I am primarily concerned with generating prospects for drilling and developing reserves, and, if I am fortunate, plans for production to operate those leases.

We have much oil yet to be found in the lower 48 States. The larger fields have been found, but now we have many small, more settled stratigraphic type traps to be searched for. And these type traps increase the risk factor considerably. Many of these little fields may cover 80 to 160 acres of area. But reserves may run anywhere from 10,000 to 50,000 to 100,000 barrels per well. And these connect to our total reserves.

The independent oil operator depends very heavily upon outside investor money for his funds to do his exploration. And without a tax advantage, the investors are reluctant to invest in such a high-risk venture. Without exploratory money, drilling ceases, all of the allied services cease, also. So it causes a rippling effect throughout the whole industry, even to the grocery store man and the other retail merchants.

Retaining the tax advantage in the tax reform is a must for investors. We are presently faced with a price decline. But even before this, we were faced with the problem of trying to raise capital for investment, faced with the tax reform, and favorable treatment would be given to the investors. We feel that our tax—our price decline is immediate and hopefully not long range. But the disadvantages in the tax reform could be forever. Once taxes get on, it seems like they never get off.

We know that the timelag for exploration from the field to the consumer may range from 1 to 2 years. It has been said that oil is found in the mind of men. But the time that it takes to generate an oil prospect and for it to reach the consumer could be 1 to 2 and possibly even 3 years. If we let our exploration lag, then when we face a crisis like we had in 1973, it takes us quite some time to be able to catch up. And it seems like we operate under crises. When everything is going fine, we sit back and go our merry way. But when the crisis hits, we all panic. This applies to our Government as well as to individuals.

I operate 11 leases and have interests in approximately 29 wells. About half of these are stripper wells. And as Mr. Chalmers and Mr. Michel pointed out, at the present price, makes it unprofitable to operate.

We feel like the tax reform bill can be most damaging of all. Most people do not understand the meaning of tax depletion. It is not a tax loophole. It was implemented by Congress, I think, back in the 1920's to encourage investments in industries which had declining resources. For example, if you were an investor with \$1 million, and you invested in a grocery store or an oil venture, say that the oil venture was successful and would produce for 10 years, and be depleted and plugged out; your assets would be zero. In the meanwhile, the grocery store, everybody eats, it is very profitable; in 10 years, you have 10 grocery stores worth \$10 million. Which one would you invest in?

This is the reason that Congress implemented the depletion allowance to encourage investors to invest in such high-risk ventures where the assets would be declining.

We feel like the unfavorable tax reform can be long range and should be eliminated. The President has talked about fairness in the tax reform. We, of all people, like to be fair in our taxes. We feel that the oil industry has borne more than its share of taxes. And I say what is fair by eliminating 10 million people off the lower end of the tax role and putting the burden on the upper group, and particularly on industry. Industry creates jobs, not Federal giveaways.

If we want to be fair, why not put a Federal sales tax across the board, no exemptions. Everybody pay their part of the taxes, including the illegal aliens, the mobsters, and everybody else. So the tax reform that is coming out of Congress is far from being fair to industry.

I did not have a prepared speech here, so this concludes my remarks. Thank you very much.

Mr. STENHOLM. Thank you, Earl.

Mr. Combest.

Mr. COMBEST. Thank you, Mr. Chairman.

Dr. HARRISON, we have made countless numbers of speeches. Certain of us have. We were in the minority vote on the tax reform legislation. We have made countless numbers of speeches that fair, simplistic, and economic growth that was supposedly in tax reform was abandoned many many months ago.

In your activities, you had indicated finding outside investors, which we all understand is a very significant part of exploration. What have you seen in the last year, in the calendar year 1985 that happened to investors?

Dr. HARRISON. Well, in the time of a normal year, I drill 10 to 15 wells per year. Presently, I have not drilled any this year to start with, not because there are no prospects; I have a number of them there in the office, the geology worked up and the leases acquired. I have some leases and time running on them. But finding a man to drill them is very difficult. So at the present time it is most difficult for us.

Mr. COMBEST. For the record, explain what you mean when you say you have time running on those leases.

Dr. HARRISON. What I mean is work up a geological prospect and then go to the landowner and secure the lease. In the meantime, this is maybe for a 1-year term or 2 years, or possibly a 3-year term. In the past, we used to get 10-year leases, but this is no

longer. Now the landowners are reluctant to even give you a 3-year lease.

As I said, the time to generate a prospect and then get the money raised and drill it, could be a year. So if you have a 1-year lease your time gets pretty short. If you are not able to raise the money and drill the well, the lease runs out.

Mr. COMBEST. One of the problems we are looking at, of course, is that there is not one simple solution to this crisis we are in. It is going to take a lot of activity. One of the things that I hope that we can emphasize as we go through this is that once the real concerns that began in the industry began in late 1984 or 1985 on the tax legislation. If we can do something to curb or change, or by some miracle that happens in the next short period of time, we still have some massive problems that we have to deal with in the Tax Code or in proposed tax legislation as it affects this industry, or many of these other things may not work in total energy independence.

How do you feel about the import oil fee?

Dr. HARRISON. It sounds like a quick-fix. But I am not really sure that is the answer to it.

Mr. CHALMERS. There are too many loopholes, I think, in an import on oil, especially if you exempt Mexico and Venezuela from any import fee. If you exempt Mexico, the Arabs will have boats landing in Mexico by the dozen, by noon tomorrow, coming right across that border at no import fee. I think you would have so many different problems, paper work; military would be exempt, hospitals would be exempt, mercenary institutions would be exempt. Heating oil would usually be exempt. Where would the exemptions stop? If you could make it a clean import fee, just clean. But look at what you would do to petrochemical plants. Look at what you would do with a lot of industries that have to compete with foreign products. You cannot lift foreign shoes and foreign fabrics and buttons and whatever else that come in here import-free, and compete with petrochemical plants that have to pay that \$10 in import fee.

So I think it is so complex that we would be better off to think of something else rather than a straight import fee. I would like that to just be a quick-fix for a few months, and then we would be in real bad shape. That is my position on import fee.

Mr. COMBEST. That is an extremely big "if" that you mentioned, and that is something that we are having to deal with; that is, if it is clean and that the exemptions, whether they be domestic or whether they be international, are of a great deal of concern as to how that may be implemented. If in fact it is only a revenue measure, I have real problems with an import fee. I assure you if that just raises revenue, it is going to be spent by the Federal Government. It has got to reach down to the level of helping the producer out without—and the regulatory agency that is going to be involved to administer that concerns me a great deal if, in fact, there are those exemptions, is the producer really going to be helped in it.

Mr. CHALMERS. The import thing, it not only stops at oil. If you are going to be fair to our country and to all industries and to all people, I think you would have to put an import tax on everything that comes into this country to make it equal to where we would be

on the same standard of living as foreign countries. I don't likely want to be that way. I just can't see it.

Mr. MICHEL. You know, Mr. Combest, I think we as independent producers have never had the occasion to put the tax on somebody else just to clear our hides. I think John probably hit on something that a lot of people feel. That is, if you are going to do it, go across the border. I for one do not want the American consumer to say, "You oil people put that tax on me and raised my bill." As far as public relations, from that standpoint, it really isn't good.

As far as the National Stripper Well Association is concerned, we have never made a policy on this for a very simple reason. We are funded primarily by the various oil and gas associations nationwide, and we leave that policy to them. We do not feel like that is in our bailiwick to take a stand on. So I have to speak to you personally as to what my feelings are.

I know in a conversation with one of the Senators from Oklahoma, he said, "If you want an import duty on foreign crude, all you got to do is kill it and come up here and support. I couldn't pass this—if you came up here and supported it." Now, I kind of feel like that is exactly true. As far as getting a clean bill, I doubt that we even have a chance. I think Congressman Stenholm may feel the same way; I don't know. I know he supports the tax. I, personally, do not.

Mr. COMBEST. That again is a major concern. What the final decision is going to be made on supporting or not supporting it is how clean that bill may be.

One of the things you pointed out in your testimony which I thought was very important, I think that the traditional industry has—in fact, I have seen national news accounts of interviews done in my congressional district with people who are in the business. Some of them say, in fact many of them say, "Well, we have had the ups and downs for years. Now it's down, it's coming back."

I guess a common thread which has run throughout the testimony these past 2 days is that this is not a usual down. We are looking at some problems here that may be the end of this business as many people know it. To me, I want to be able to continue to impress upon those people whom I deal with that this is a different situation this time that has got to be dealt with in order to keep it surviving as we know the business today.

Thank you, Mr. Chairman.

Mr. STENHOLM. For the record, I do support an oil import fee. I supported it in March 1985. Dr. Harrison, I agree with your assessment; as a quick fix, it is not an answer. The problems with doing it on a short-term basis are very real, John. I still believe that it should be a necessary part of a national energy policy in order to provide stability. It has worked in other industries. We use it in automobiles, we use it in wool, we use it in peanuts, and in so many other commodities.

But to clarify my position on it, I supported it over a year ago because I believed that Sheik Yamani would flood the market with cheap oil. I believed then and believe today that an oil import fee would help provide price stability. It is not going to happen, so we do not need to spend any further time discussing it.

Mr. Michel, you indicated that you had received telephone calls. I am particularly curious as to what type of call you would receive from the Department of the Interior and the Department of Defense.

Mr. MICHEL. These were very interesting calls, Congressman, because the primary thing Interior called me about was to determine did we have 30- and 60-day clauses in our leases that would force us to return these leases to the landowner and cessation of production. I assured him we did. He said, "We in Interior are now trying to perfect some way to keep our producers, who are having to cease production on Federal lands, from having to return those leases to the Federal Government." In other words, an extension of that time limit.

If we should get that, it would be a very precedent-setting factor for us out here in the field. I only brought this up because I thought maybe you and Mr. Combest and other Members of the Congress should know this; maybe you already knew it, that they were working on this, and probably urge them to do it. Because for those people who do operate on Federal lands, it would really be a help, a great help to keep them from losing those leases.

As far as the Defense Department was concerned, I had almost an hour-and-a-half conversation from people in Defense—thank goodness, on their nickel. Their whole bag was, "We are concerned about the loss of reserves from marginal wells. What is your best judgment on what we will lose, how many wells will be abandoned, how many wells will be plugged?" And we went through this scenario for, as I said, a good hour and fifteen minutes, to an hour-and-a-half. They are trying to help, but I don't know how. And I think that is the reason I wanted to discuss it with you gentlemen.

Maybe in your efforts over there in Defense, you can assist them in trying to find out some method to keep us from having to lose these barrels of reserves; whether it is 2, 2½, 3 billion, whatever it might be. It could be even greater than that, I assume.

But they are concerned, and I think the primary thing I am driving at here is that there is recognition in the various agencies and the Congress that there is a problem out here. I think that is the first hill to climb.

The second one is to followup on it, and I think that is where you gentlemen come in.

Mr. STENHOLM. To follow up on that, with concern being expressed by the Department of Defense, how does this square with the administration's proposal to sell the Naval Petroleum Reserve at this point in time to private enterprise? Do you see any inconsistency in that?

Mr. MICHEL. You mentioned something awhile ago that did strike a nerve, and that is—John, I think mentioned it, as to a subsidy or having the Government buy this oil and put it in the SPR. I am not sure I agree with the Government buying the oil and putting it in the SPR. The Government always has a way of screwing things up when they do move oil. Why not leave it where it is? It is very safe and secure where it is, but this may be where the Bentzen-Wallach bill comes into play, where you do put a floor there on those wells that produced economically the last half of 1985. Make it a part of the SPR, but leave it where it is.

When the Governor's Office called me, they asked me what I thought the real price of a barrel of crude should be. And I told him someplace in the neighborhood of \$22 to \$25. And then he questioned me as to why. I gave him four reasons, Mr. Chairman.

At that price, maybe \$20 to \$22—I told them \$22 to \$25—our people in the field are able to carry on some semblance of an exploration program. Our consuming public had already had a cut in the price of their product down to some lower level than they were used to paying. At that particular time, our interest rates had pretty well leveled out. Our producers who had a heavy debt load were able to meet their obligations at our financial institutions.

Those were four of the reasons I gave him why I thought the price of crude should fall in that category. And I still think that is—maybe it's \$20 to \$22; I don't know what it is. With this curtailment in our lifting costs, by the things that John and Earl and all the other producers are doing, by cutting salaries and all these other things, maybe that is the real price. But that is the figure I gave our Governor's Office after three conference calls to them. They are extremely worried about their revenues down there, as you well know.

But I do not see taking this oil out of the ground and moving it to someplace else, and particularly to the SPR, because when it comes time, the time of need, I do not know what the deliverability capabilities are to the various refining segments scattered throughout this Nation. It may not be possible at all.

Mr. STENHOLM. Mr. Chalmers, you were advocating quite forcefully and articulately the need for more tax incentives. Both you and Dr. Harrison are undoubtedly aware that that flies directly in the face of what the President and the administration are asking the Congress to do in the area of tax reform. If it had been left up to Mr. Combest and me, we would have already laid to rest the possibility of changes in the Tax Code because of the impact on the oil industry. Unfortunately we were unsuccessful in doing so.

It is difficult talking to our colleagues in the Congress about oil and gas tax incentives, and it is almost impossible to talk about increased incentives when the administration is going in exactly the opposite direction. Do you have any suggestions as to how we might proceed to do this?

Mr. CHALMERS. The President of the United States and Congress has to recognize the dilemma that we are in. We are headed for a calamity on oil. Three years from now, 4 years from now, we are going to be producing about 35 percent of what we need. When that situation comes, don't you believe that Mexico is going to give us cheap oil. Don't you believe that Canada or Venezuela is going to do it. They are going to join hands with the Arabs. The United Kingdom will do the same thing. When you start flashing that green, there is a lot of difference in \$14 oil and \$32 oil. They will join with the Arabs. We are going to be sitting over here needing 65 percent of our daily needs from Canada, Mexico, and 50 percent of what they do from the Arab countries. If Congress and the President do not recognize that, and they cannot see that now is the time to start taking steps, we are in terrible shape. I think you as a Congressman, and your cohort there, and other Congressmen

should do the best that you can to lay out the problem in front of the Congress and the President of the United States.

Now, I voted for Mr. Reagan, but I'm not going to do it again. He has turned his back on the oil operators and he has turned his back on industry in this country that depends upon energy for fuel. If he cannot see it, we are in terrible shape. If we do not have enough Congressmen and Senators up there to convince him that we do have, then we had better get rid of the whole damn bunch.

Mr. STENHOLM. I am glad I'm running unopposed. You have a point there.

John, I want to commend you for your honesty. If someone were to have told me a year or two ago that I would be conducting a hearing during which individuals from the oil industry would testify as to the need for Federal help, I would have said that was highly unlikely. The fact that you are honestly and openly asking for Federal help is an indication that the industry recognizes the seriousness of the current situation. It is our challenge to bring the story to our colleagues on Capitol Hill, and that is why we are here today. We will formulate a hearing record and develop a method of bringing the story to Washington, emphasizing the national security implications. I was very interested to learn of the call from the Defense Department regarding stripper oil, because this is a matter of national security. In agriculture and in the energy industry there are tremendous difficulties in putting together a national policy. These industries and our own United States are a part of the world economy, and working within that framework is not easy.

Mr. MICHEL. Congressman, I know that neither you nor Mr. Combest were in the Congress in 1969. I happen to have had the privilege of testifying with A.V. Jones before the House Ways and Means Committee on the 1969 Tax Reform Act.

Should we pass a tax bill, the House-Treasury Two, I believe, Treasury One; I think we are going back to the same thing we did to ourselves in 1969. And I do not know whether you realize all the facts and figures that go with this. But in 1970, our Nation's rig count got to 837 rigs. In 1970, we did not explore. In 1971, we did not do a darn thing in our exploration in 1972. And you know what happened in 1973. We all shaped up at the gasoline lines.

Fortunately, at that time, we had enough reserves to pass through this, that kept it from being any worse than it really was. But I hesitate to think what will happen the next time, at the next embargo time when we do get 65- or 70-percent dependent because we are not going to have the reserve capacity to make up for it. I see gasoline prices in the \$2 range or above. I am looking down the road maybe—I don't know when; I don't know when it will be. Maybe Dr. Fisher knows the exact date; I certainly do not. But surely as I am sitting here, this is a possibility that will happen, and I hate to see it happen to this Nation. Most of all, I hate to see us as a nation not the masters of our own foreign policy because of the lack of energy in this Nation. I think the only way out of it: Open up Federal lands, Federal offshore, basins in Alaska, let us explore them. I think that is where we are to come out of this thing if we are to come out of it.

Dr. HARRISON. Mr. Chairman, I do not think it is so much that we need Government help as we need the Government to get out of our way in putting the stumbling blocks in our way, with the rules and regulations, windfall profit tax, and so forth.

I am not knowledgeable about international politics. But I think one thing we can do is quit trying to solve all the problems of the world with giveaways and take care of our own. The President is proposing to give the Contras \$100 million, while at the same time we are foreclosing on our farmers. Charity begins at home. I think it is time we stop trying to solve the world problems with our almighty dollar.

Mr. STENHOLM. With all due respect, I agree with Mr. Chalmers' statement. I think right now there is Federal help needed. And I believe there is some Federal help that is needed, both in agriculture and in other areas.

Thank you, gentlemen, very much for your time and testimony today. It was very helpful.

I call the final panel: Mr. Bud Darby, Mr. John Slaughter, and Mr. Norman Naill.

Mr. COMBEST. Gentlemen, thank you. In the brief absence of Chairman Stenholm, we will go ahead and begin.

Mr. Darby, if you would start, please?

TESTIMONY OF BUD DARBY, CRESCENT SUPPLY CO., ABILENE, TX

Mr. DARBY. Thank you. I am Bud Darby, general manager of Crescent Supply Co., which is a small locally owned supply store in Abilene. We have a group of investors in it; all of them are local.

We have annual sales, or have had, of approximately \$5¾ million. The average workforce over the last 3 years was 15 people, 16 variables.

The obvious effects that we have experienced from the fall of the oil prices is that our sales are down about 57 percent from what they were in the last 6 months prior to March 1. Approximately 50 percent of it comes from new wells and 50 percent of it from reworking old wells, stripper wells, water floods, such as this right here. Consequently, with the price being what it is, they are not doing either one. They are not drilling the new wells and they are not reworking the old wells, which has forced us to cut all overhead. We have cut our workforce down approximately 25 percent. There is a good chance that there will be more cuts at the end of this month. We have cut out a lot of the employee benefits so that we can maintain in the black while the slowdown is here. We have cut out all the insurance and commissions, sick leave; we are not supporting any FFA organizations, Boy Scouts, or cheerleaders or any of that that come by.

There is no true sign right now as to when it is going to turn around, what it is going to take to help us out. We are having a great problem with our collections. Most of our oil operators now have pledged their oil runs to the bank. And with the price falling the way it is, their bank payments have not fallen. So they turn back to us. Our accounts receivable is down approximately 27 percent of what it has been.

The last 6 months prior to March 1, 79 percent of all accounts receivable have been under 60 days old; have been from zero current to 60 days old, with 21 percent being over 60 days. Since March 1 through now, our accounts receivable, 44 percent is under 60 days old and 56 percent is over 60 days old. These are good people. It is not shim-shams out of Dallas. These are people who are good. They just flatly are committed to the bank.

I was visiting with one of our creditors, people who owe us money, last week. And he negotiated a \$50,000 loan with the bank in January. His oil run was \$5,000 a month. On that basis, he was basing it on \$18 oil. He was paying \$2,500 a month to the bank, leaving him \$2,500 a month to pay pump repairs and the suds. Now days, his oil run is \$3,000 a month. He still has to pay \$2,500 to the bank. That leaves him \$500 to pay the pumper, electricity bill, and then comes old Bud. It makes it tough. And that is our problem. We do not know exactly what it is going to take to turn it around. Hopefully the price of oil will come around. Until then, nothing is going to help it.

That is our situation in the whole.

Thank you.

Mr. COMBEST. Thank you, Mr. Darby.

Mr. Slaughter.

**TESTIMONY OF JOHN SLAUGHTER, DISTRICT MANAGER,
SUPERIOR SUPPLY CO., ABILENE, TX**

Mr. SLAUGHTER. Thank you for this opportunity to appear before this subcommittee.

I am John Slaughter, district manager of Superior Supply Co., a major oilfield supply company. Our sales area covers most of west central Texas. Our local supply store is oriented mostly to production equipment, which includes oil country tubular goods, vessels, pumping units, and fittings.

Since the first of the year, our volume of business has fallen at least 50 percent, and in the last month it has fallen another 10 percent. At one time, we had 32 employees locally. Today, we have 12. This next month will determine whether we will have another reduction in our workforce. Our survival is dependent upon mostly used equipment sales and repairs to subsurface pumps. Our present inventory of oil country tubular goods is based on prices of 3 months ago. Today these same goods are cheaper due to the flooding of the market by people reducing their inventory.

The cash-flow of our local operators has been cut in half, and they are having a difficult time in servicing their debts as well as in selling their prospects. Our business is dependent on their activities. Some operators are shutting down marginal wells to cut their overhead. This in turn affects our business. I see no relief in the near future. I am concerned that the local economy, because of the depressed oilfield business may hurt all businesses, down to the local corner grocery store.

I have been in the oil service business 37 years, during which time I have seen cycling and instability, but not to the extent that we have experienced in the last 3 months.

Thank you, sir.

Mr. COMBEST. Thank you, Mr. Slaughter.
Mr. Naill.

**TESTIMONY OF NORMAN E.C. NAILL, VICE PRESIDENT AND
GENERAL MANAGER, SUN SUPPLY CORP., ABILENE, TX**

Mr. NAILL. Thank you.

It is a privilege to appear here today. And I want to especially thank each of you for dedicating the time and effort necessary to make these visits into this important area of our country to measure conditions from the perspective that you can get only by being on the scene.

I am Norman Naill, vice president and general manager of Sun Supply Corp. Sun Supply Corp. is a family-owned business which was founded and has operated in Abilene for nearly 65 years. Its business is in two basic fields: The wholesale distribution of electrical materials used in the building industry and commercial wiring endeavors; and in the wholesale distribution of floor covering materials. Abilene is the headquarters, and a branch operation is located in Lubbock. We employ about 40 people in such areas as sales territory representatives, inside counter sales people, warehousemen, long haul and local delivery people, and the obvious clerical and administrative people to support these.

We are a small business of annual sales of under \$5 million. Our two locations serve customers from southeast New Mexico, through the Texas Panhandle, the Permian Basin area, and of course the Big Country area around Abilene. Each of these areas has experienced significant contributions from the oil and gas industries as it exploded in recent years and have, therefore, been a large factor in the growth of our business. Conversely, as the oil and gas industry has contracted, so has the business of our customers.

The effects on our two types of customers, the electrical contractors and floor covering dealers, have really not been much different. Their reactions to the oil and gas economic decline have been different, and you may be interested in our perception of these reactions.

Our electrical contractor customers are concentrated within about a 60-mile radius of Abilene. Over the last 9 to 15 months, we have had numerous customers close or cease operating their businesses, go to work for other contractors, or leave the area. The new home construction business had already experienced a slowdown because of the high interest rates and the phaseout of the B-52 operation at Dyess Air Force Base.

When the oil and gas decline started, it seemed to be the proverbial straw that broke the camel's back. Many people in Abilene had learned to rely on a second income from a source other than actual employment. That is, they are retired military, perhaps, or have some oil income from either royalties or production participation. Everyone tends to grow accustomed to their income, whatever it is. A significant downward change is very difficult to cope with, especially if the recipients need those dollars for maintaining a debt-heavy way of life. A domino effect can be disastrous when one important source of monthly income disappears. And if that source disappears from a large group of people all at one time, then their

list of options becomes very short. That is, if I were to lose a royalty income and yet have debt obligations to service from that anticipated income, then I would need to make other arrangements for handling those obligations. If additional working hours were not available because of a slowdown in work needs, and lending agencies tightened their restrictions because their operation was curtailed by the same loss of income as mine, then I may not have many ways to replace that lost income and fulfill my obligations. And when I do not fulfill my obligations, that dominoes into those I owe not fulfilling theirs.

It is a vicious rapid cycle that comes when one very important segment of an economy permeates so many lives, habits, and standards of living.

The floor covering dealers that we serve are over a larger geographic area than our electrical contractors. But they still were in the same general area in which there has been such a demise in the oil and gas industry.

Coupled with that problem is the large agricultural influence in our panhandle area. These dealers have now learned to operate with less inventory, and by buying as they sell rather than stocking materials. Mom-and-pop operations have become momless or popless in many cases, as one spouse tries to work outside the business in order to help overcome the slowdown in sales. Collections have become much more difficult.

West Texans do not like to ask for payments of accounts. They have been accustomed to operating on a handshake and a good-faith basis of payment upon completion of jobs. But now customers, often with the best of intentions when they buy, find that by the time payment is due that their circumstances have changed so that they can no longer pay promptly. The store then finds itself in the collection business and that detracts from the regular business of sales and service.

What we are back to, of course, is simply another vicious circle. If I cannot pay you, you cannot pay your supplier, who cannot pay his manufacturer, who cannot pay his payroll or his tax bill. It is a web spun by a deceptively simple cause, a slowdown in oil and gas production because of a decline in the oil price which makes the production unprofitable.

Profit must be possible in any business. Perhaps the oil industry has grown accustomed to profits too great or too easily acquired. But I think we all agree that high risks deserve high gain because it is easy to have high loss. I would hope that some of the creative minds available in this great country will be able to devise a way to put to work the tremendous stockpile of drilling rigs and talented people expert in the exploration and production of oil and gas in order to get this area's economy on the move again and, ultimately, to get this country into a position of significantly less dependence on foreign oil and gas. There must be a way to make it profitable to drill. There must be a way to work the large capable workforce that has been idled. There must be a way to sell this production that would come from this working force. The chain reaction will work just as surely as we begin putting these forces back to work as it has when we put them out of work.

Then as this oil and gas industry redevelops—and, gentlemen, this cannot be a long-range program, but one that needs to be implemented quickly—we must also build on longer range planning to diversify this part of the country even further into other areas of business activity. Oil and gas, while very logically will be a large factor in our economy, should be a lesser percentage of the total than it has been in the past. That is not to say that we should diminish oil and gas contributions; rather, we should increase some of the other areas to be larger contributors to the overall economy.

We have often as a country decided what we must do in a foreign country to support a government, or resist a movement, or to reinforce an effort through material or financial aid. The case has often been very persuasively built that this action was for our own good in the long run, for the security of our country, or for its long-range goals. But now I believe we must look inwardly quickly. We must somehow overcome the bias between geographic sections of our country in determining what is good for the whole. We must understand ourselves and make all our citizens understand the importance of the oil and gas industry; not to Abilene or west Texas or even to Texas, but to the United States and what this great country means to each of us and the world. We need not worry about giving foreign aid or supporting some remote distant government if we cannot somehow bolster our own needs. And it is unthinkable to visualize ourselves in need of foreign aid from others some day, and probably even more unthinkable to believe that many countries would even favor us with foreign aid if we needed it.

I certainly do not subscribe to isolationist theories, but we must somehow take care of our own first. We have been disappointed many times by friends. We cannot afford now to support fair weather friends if we cannot support our own. We must vitalize and revive the oil and gas industry, and soon, in order to have the thriving economy that the United States of America must have to continue to be the significant country that it deserves to be.

Thank you for your attention.

Mr. STENHOLM. Mr. Combest.

Mr. COMBEST. Thank you, Mr. Chairman.

I have on a number of occasions, and basically have related it to agriculture over the past year in developing farm legislation, indicated that we have got to have some type of long-range agricultural policy. I think it parallels to this problem as well. We have got to have a long-range energy policy.

I do agree with you, however, Mr. Naill, that it is important that we do something on an immediate short-term basis, as we must in agriculture, to keep people in business. Then in the future they can be there to hopefully reap the rewards of what may come with the long-range policy.

I can also relate to your statement very closely. In my previous occupation, I was in the wholesale electronics business, covering much of the same area as you did. And it has been very obvious to me for that period of years, as you can see certain areas, as their economies moved, our business moved. Our accounts receivable moved, and many of them ended up moving.

It does have the ripple effect. It has a very strong effect on so many businesses that are either directly or indirectly related to the business. And again, as was expressed earlier, I think this is very important to see how it is that it affects other types of business rather than just that producer, which I think too many times we have a tendency, or at least people in general have a tendency to try to concentrate on just the producer himself. It is going to affect the whole economy of west Texas.

Have you all experienced the same—or the other two of you—have you experienced the same things that Mr. Darby had indicated as a trend over the past few months on accounts receivable?

Mr. NAILL. Yes. Very definitely.

Mr. COMBEST. Have you lost a significant number, given a trend over many, many years, comparing a significant number of people who have completely gone out of business?

Mr. NAILL. We have experienced a number of small companies closing or going to work for other contractors, or leaving the area; and, unfortunately, sometimes in debt when they leave. And we have had larger write-offs of bad debt or noncollectibles or very doubtful collections in the last year than we have in the history of our company.

Mr. SLAUGHTER. I think there are many of them who are going to fall by the wayside. They do not have any money. They owe people; owe banks; owe supply stores; and owe the other service companies. There is no way they can stay.

Mr. COMBEST. One of the things that becomes very obvious to those of us like the chairman and myself, who travel a great deal over a fairly good geographic area and a lot of towns that range in size from very, very few people to fairly large cities, can see a continual change in those towns. We have some very small cities, very small towns that will have either a primarily agricultural or energy or some that have a mix, and there are stores that are closing on the streets of those towns that have been there for 20 or 30 years, family operations. Those stores will never come back. They may employ 4, 5, 6, or 10 people; but they are part of that community and have been a part of that community. And as we see that type of deterioration and erosion, I don't know what is out there that is going to replace it.

A point you made in your testimony with which I strongly agree, Mr. Naill, is that if we do not do something on a short term, I do not know if we can ever reverse the trend and come back to basically the way that we know rural life; whether it is in Abilene or in Odessa or Lubbock.

Mr. NAILL. You nearly made an analogy there that I think would be appropriate here in our small businesses of one, two, and three employees to our stripper wells. They will never come back; you're right. Shut them in and they are gone. And I think they are just as important as I certainly agree the stripper wells are.

Another really detrimental thing is the distraction caused to management and sales people in this collection problem. I, personally, spend probably 40 to 50 percent of my time today on credit and credit-type problems. And this is not really the most productive way to have our company grow. And mine is not a unique situation, I am sure.

Mr. COMBEST. One other personal note, and I will turn it back to the chairman, is that when I closed my business in 1983, in the period of time I had built customers up, 8 of the 10 largest customers that I had—it was a very small business—are no longer in business. And those things become very personal, and you can see the effects of that very quickly.

I appreciate your testimony, gentlemen.

Mr. STENHOLM. The challenge to us in the Congress is to be very careful how we choose our words and consider the ramifications of our legislation on the everyday lives of Americans.

I apologize for being out of the room, Mr. Slaughter and Mr. Darby, during your statements. Are you experiencing any problems with our bankruptcy laws, and how are they affecting your customers? Are you aware of any problem there? And do you have any comments regarding the cost of liability insurance and that whole controversy? I would welcome your comments in either of those two areas.

Mr. DARBY. On our liability insurance, we were forced to cancel it. It went from \$7,000 a year to approximately \$23,000 on product liability, with the umbrella policy going from \$500 a year to between \$5 and \$10,000. They could not give us an exact price until the day we wanted to purchase it. All they would give us is between \$5 and \$10,000, and there was no way we could afford it. Our lawyers told us we were fools to be without it because if we had a case we would lose the whole company. And we told them we were going to lose the whole company if we had it; we didn't have much choice.

Mr. NAILL. It is a very cruel kind of thing. We kind of bellied up to it and took it, but we should not have. We cannot afford it either.

But the interesting thing is that the insurance companies really do not care if you take it or not. They are really not too interested in insuring you, because they have their problems, too, I'm sure. But you would have to be able to find it at a price. No. 1, if you can afford it. So the cost of doing business through insurance, and in the legal fees for these collection things, has drastically risen in our business.

Mr. SLAUGHTER. Regarding the bankruptcy, we have three local bankruptcies which affect my company—about half a million dollars. We do not ever expect to get any of that money. They will just reorganize and keep operating.

Mr. DARBY. May I add one note on the bankruptcies?

Mr. STENHOLM. Surely.

Mr. DARBY. In the 6 years I have been personally involved through customers, close to 20 to 25 bankruptcies. Some of them had assets, just no cash; but to this date, we have never yet received one penny, on anybody that has filed chapter XI reorganization, or chapter VII. And like I said, this is over a 6-year period that I have personally seen this. We have yet to receive one cent, even if it went from chapter XI to chapter VII, or stayed in chapter XI. It has yet to ever get back to the actual creditors of the person filing chapter XI.

Mr. STENHOLM. I would judge by all of your very brief answers that there are some severe problems, with the application of cur-

rent law as it applies to bankruptcy, and I know there are problems with the liability insurance question.

This subcommittee held a hearing in Portsmouth, VA last fall on this subject, as it pertained to energy companies. We found there are problems throughout all businesses, and these problems must be dealt with. I am reluctant to see Federal intervention in this area, but it may be that we are going to have to have some kind of Federal intervention to achieve a resolution to the current situation.

Thank you, gentlemen, very much for taking time to testify today. We appreciate very much your being here.

Now we have some requests to make some unscheduled statements. I would ask that Mr. R.B. Terrell, Mr. Dick Anders, and Mr. Gene Boone take your places at the table. We would be glad to hear your statements at this time.

Mr. Terrell, please identify yourself and who you represent. I understand you have a statement to submit. It will be made a part of the record, as you requested.

TESTIMONY OF R.B. TERRELL, PRESIDENT, MIDTEX ENERGY, INC., LUBBOCK, TX

Mr. TERRELL. Thank you very much.

I am R.B. Terrell. I am a small independent oil and gas operator involved with three corporations, Mid-Tex Energy of which I am the president; and Texas Corporation; and then Tamco Energy, a California corporation of which I am vice president; and then Hartel, Inc., of which I am president, a Texas corporation.

Together, three small corporations, we are operating some 70-odd wells of which most of them, all except 5, and possibly just 3, will be shut down in the next few weeks unless something changes.

I had an oil and gas analyst in Houston run some figures for me, which is what I have submitted, production of 3 barrels, 6 barrels, 10 barrels, and 15 barrels a day. And it was amazing to me. I knew I was losing money on a lot of the wells, but I did not realize how much until I got that analyst. And he did not take into fact the insurance problems that we are having.

My figures on the Texas wells is a little different from Mr. Michel's. The Railroad Commission figures that I have, we have 212,000-plus wells in the State of Texas, of which 142,000-plus are stripper-type wells; that is 10 barrels or less. The figures that the oil and gas analyst ran in Houston showed a loss of 15 barrels a day at \$16 oil. According to that, we are going to have less than 70,000 wells, possibly in the neighborhood of 50,000 wells, only, in the State of Texas in the next year if something is not changed.

Now, I do not know what all ought to be done. I know the Natural Gas Policy Act of 1978 should be repealed, because it is an unfair thing whenever we are regulated at the well-head, and nobody regulated between the well-head and the end user. The Census Bureau reports that between 1978 and 1983 electricity in the average home rose from \$35 in 1978 to \$56 in 1983 a rise of 60 percent and gas rose 72 percent from \$29 to \$50 per month while we at the wellhead were reduced in price from something over \$3 to less than \$2 per MCF. The pipeline companies making the big

excess profits which caused them to break up into many corporations, taking their excess profits and buying Case and International Harvester Companies as well as many more money losers that had many millions of dollars of loss carry forwards. I have one well that we drilled this year that is covered by the windfall profits tax. The rest of them are not.

We have problems, but I do not believe the oil and gas industry, or the farm industry, the steel industry, the shoe industry, or the clothing industry have any different problem. We all have the same problem. And that problem is the Government's give-away of American business and money.

I have been in quite a session with Phil Gramm. In fact, I got two letters from him 2 days apart on our problem. And I do not understand why Government cannot understand that there is absolutely no way that we producers in the United States can have the high economy, the high living standards, pay the highest wages, pay all the taxes, and compete with non-taxed imports. A lot of them made with slave labor, coolie labor, and peon labor. It is an impossibility, but nobody in Washington seems to understand.

Now, I think that we have present laws right today that can handle the job that are not being instituted. We have an antidumping law in this country which prevents foreign countries from dumping goods in this country at a loss to us, where it takes our businesses out of it. And that law is being completely overlooked by government, this antidumping law. If this law does not cover everything that is imported then you should make it do so.

Now, the Mexicans, which I am acquainted with, are scared to death of it in the area of importing cement, which they would like to take over the cement industry in the United States. They have the stuff to do it with down there. But they are scared to death of the price. They would like to put it in here, cement in here at \$30-odd a ton, when our present prices are running about \$70. But they are afraid to because of the dumping laws. But none of these foreign countries that are importing oil is afraid of it.

And it has gotten to a ridiculous stage, really, because I am just a pee-wee. Yet I had a man call me representing a foreign country that had solid contracts for 300,000 barrels a day, wanting me to sell it for him. I said: "What do you need me for?" Just needed an American citizen. I don't know why. But they would not even put a price on it. They said: "You see what you can get for it under spot price, and let us know and we will take it." And I found out since that one of the small Arab countries contracted their oil for \$8 a barrel to this country.

A few months ago, Mobile, Texaco, and Exxon made an under-the-counter deal with Saudi Arabia, and nobody knows what they are getting.

Now, these multinational companies are doing better than they have ever done. They are happy. Gasoline has gone down 30 percent and oil over 66 percent. That leaves quite a spread for them above what they were normally making before. I think we need one law passed in Washington, and that is a law that it is a capital offense for a PAC or a lobbyist group to represent a multinational corporation or a foreign country. That will solve a big part of our problems.

We have less than 1,000 elected officials in Washington, DC; yet Saudi Arabia has 3,000 energy lobbyists in Washington, DC. I cannot understand it. I know that you Congressmen are human. And if somebody dropped \$100,000 or \$200,000 in your campaign fund, you cannot do anything but lean toward them. It is an impossibility because we are just humans. And that has got to be stopped and get back to the American people, or I do not know what is going to happen.

I get to watching C-Span, and I get rather perturbed because I think after watching it awhile I think of Alvin Töpper's book, "Future Shock," where he says that our Government is obsolete to the fact that when we have a problem it becomes a major catastrophe before it can be solved. And it kind of looks that way when you watch C-Span.

But I believe that we have on the books a law, this antidumping law, if it is enforced. However, after talking with Donald Hodel and listening to John Harrington, I do not believe they are capable of instituting any kind of a law because they absolutely do not understand the problems of the American people, the producers of this country. It seems like Washington wants this country to be a consuming nation only. We cannot be a consuming nation only. Our production has to produce, but we cannot produce, and pay the taxes, and pay the wages that we have today, and compete with tax-free imports.

For instance, take the Yugo-Car; 9,000 of them hit the port in New York City. Sold for less than \$5,000 each, tax free, made by Yugoslavia, a Communist country, probably with slave labor. Is that fair to our American automobile manufacturers?

The same thing is happening in the oil industry. We are just a little later than the rest of them in hitting it. The farmers have had it for quite a few years.

But I do not know the answers, all the answers. But I know from what I hear and what I get from Washington is that Gramm-Rudman Act is going to solve all the problems. Well, I am here to tell you that the Gramm-Rudman Act will not take care of 25 percent of the tax loss that the IRS is going to have as a result of these imports. It will not take care of 25 percent of the import deficit which we are having, which runs \$17.4 billion in December. And it is not going to lessen, it is going to get more. These people are not dumb overseas. They are going to load us down with goods as long as they can get it in here at what they are doing now. And I would strongly suggest that we need to enforce this antidumping law that we already have on the books.

The foreign countries are afraid of it. They know it is an effective tool. But we are sitting here refusing to use it.

I appreciate the chance to talk on this. And I hope that that statement that I had the oil analyst make in Houston will be entered into the record because I think it is accurate. Thank you.

[Oil and gas statement of Mr. Terrell follows:]

PREPARED STATEMENT OF R.B. TERRELL, PRESIDENT,
MIDTEX ENERGY, INC., LUBBOCK, TX



R B TERRELL
PRESIDENT

3203 A 66TH ST
LUBBOCK, TX 79413
(806) 797-2681

23461 SOUTH POINTE DRIVE
SUITE 155
LAGUNA HILLS CA 92653
(714) 859-0731

Estimates of well head net back to the independent producer for West Texas Intermediate, Kern County (typical heavy California onshore) and Alaskan North Slope crude oils have been completed. These estimates covered cash only, cash plus three year workover amortization and leveraged effects.

SIGNIFICANT CONCLUSIONS ARE:

1. On a cash only basic, at \$16.00 posted price for WTI, each well must produce a minimum of 6 BOD to break-even.
 2. Including amortization cost for workovers, each well must produce a minimum of 10 BOD to break-even.
 3. If the production is leveraged (has a production loan against it) the minimum break-even rate is above 15 BOD.
 4. On a cash only basis, at \$12.00 posted price for Kern County, each well must produce a mininum of 10 BOD to break-even.
 5. Including amortization cost for workovers, each well must produce in excess of 15 BOD to break-even.
 6. Alaskan North Slope net backs to the well head about \$7.00/B (6.86) based upon parity with WTI in the USGC. Adminstratrative and other internal major oil company cost are very difficult to estimate. However, previous informal conversations have developed a range of between \$5.00 to \$8.00/B break-even total cost, depending upon the field. The levels illustrated in Table 6 indicate that some ANS production will be shut in before major well workover costs are incurred. These calculations indicate the break-even production rate for the two major onshore United States crude oils is between 10 and 15 B/D at the assumed prices and cost. This dosen't seem like a very high production level. However, it should be noted that 15% of TOTAL United States onshore and offshore production is 3 B/D or less. Average United States well production was 15.4 B/D in 1981. Which is the latest data available.
- It is unlikely, this average has increased since 1981. United States production consist of many wells that produce less than 15 B/D and very few that produce more than 200 B/D. (One estimate is that there are 620,000 + wells in the United States and that 72% of them produce less than 10 BOD.)

Based upon API data, Table 8 is an estimate of probable U.S. production loss during the next 18 - 24 months, if crude oil prices hold at levels assumed in this analysis. This data project a loss in U.S. production of approximately 2,500,000 BOD. However I believe this to be on the brighter side.

This analysis is only a brief study of what should happen to United States crude production. The analysis may not be absolutely correct, however, it is directionally correct.

These statistics were gathered and put together by
Mr. Dan Davis (Oil & Gas consultant) of Houston, Texas
Pho: (713)-440-3285

TABLE 1

WEST TEXAS INTERMEDIATE, \$/Day				
PRODUCTION, B/D	3	6	10	15
PRICE, \$/B	<-----\$16.00----->			
REVENUE, \$	48.00	96.00	160.00	240.00

ROYALTY	9.00	18.00	30.00	45.00
SEVERANCE	2.21	4.92	7.36	11.00
GATHERING	3.75	7.50	12.50	18.75
ADMINISTRATIVE	7.20	14.40	24.00	36.00
LOCAL TAXES	2.40	4.80	8.00	12.00
ELECTRICITY, 50HP	58.00	58.00	58.00	58.00

TOTAL EXPENSE =	82.56	107.62	139.86	180.75
GROSS REVENUE =	-34.56	-11.62	20.14	59.25
WORKOVER @ \$20,000.00	21.45	21.45	21.45	21.45
DEBI SERVICE	14.40	28.80	48.00	72.00
SUBTOTAL	(70.41)	(61.37)	(49.31)	(34.20)

TABLE 2

WEST TEXAS INTERMEDIATE, \$/DAY

PRODUCTION, B/D	3	6	10	15
PRICE, \$/B	<-----\$16.00----->			
REVENUE, \$	48.00	96.00	160.00	240.00
ROYALTY	9.00	18.00	30.00	45.00
SEVERANCE	2.21	4.42	7.36	11.00
GATHERING	3.75	7.50	12.50	18.75
ADMINISTRATIVE	7.20	14.40	24.00	36.00
LOCAL TAXES	2.40	4.80	8.00	12.00
ELECTRICITY 25HP	29.00	29.00	29.00	29.00
TOTAL EXPENSE =	53.56	78.12	110.86	151.75
GROSS REVENUE =	-5.56	17.88	49.14	88.25
WORKOVER @ \$20,000.00	21.45	21.45	21.45	21.45
DEBT SERVICE	14.40	28.80	48.00	72.40
SUBTOTAL	-41.41	-32.37	-20.31	-5.15

TABLE 3

WEST TEXAS INTERMEDIATE, \$/DAY

PRODUCTION, B/D	3	6	10	15
PRICE, \$/B	<-----\$16.00-----			
REVENUE, \$	48.00	96.00	160.00	240.00
ROYALTY	9.00	18.00	30.00	45.00
SEVERANCE	2.21	4.42	7.36	11.00
GATHERING	3.75	7.50	12.50	18.75
ADMINISTRATIVE	7.20	14.40	24.00	36.00
LOCAL TAXES	2.40	4.80	8.00	12.00
ELECTRICITY, 50HP	29.00	29.00	29.00	29.00
TOTAL EXPENSE =	53.56	78.12	110.86	151.75
GROSS REVENUE =	-5.56	17.88	49.14	88.25
WORKOVER @ \$50,000.00	53.50	53.50	53.50	53.50
DEBT SERVICE	14.40	28.80	48.00	72.00
SUBTOTAL	-73.46	-64.42	-52.36	-37.25

TABLE 4

WEST TEXAS INTERMEDIATE, \$/DAY

PRODUCTION, B/D	3	6	10	15
PRICE, \$/B	<-----\$16.00-----			
REVENUE, \$	48.00	96.00	160.00	240.00
ROYALTY	9.00	18.00	30.00	45.00
SEVERANCE	2.21	4.42	7.36	11.00
GATHERING	3.75	7.50	12.50	18.75
ADMINISTRATIVE	7.20	14.40	24.00	36.00
LOCAL TAXES	2.40	4.80	8.00	12.00
ELECTRICITY, 50HP	58.00	58.00	58.00	58.00
TOTAL EXPENSE =	82.56	107.12	139.86	180.75
GROSS REVENUE =	-34.56	-11.12	20.14	59.25
WORKOVER @ \$50,000.00	53.50	53.50	53.50	53.50
DEBT SERVICE	14.40	28.80	48.00	72.00
SUBTOTAL	-102.46	-93.42	-81.36	-66.25

TABLE 5

HEAVY CALIFORNIA ONSHORE: KERN COUNTY

PRODUCTION, B/D	3	6	10	15
PRICE, \$/B	<-----\$12.00----->			
REVENUE, \$	36.00	72.00	124.00	180.00
ROYALTY	6.75	13.50	22.50	33.75
SEVERANCE	1.80	3.60	6.00	9.00
GATHERING	3.75	7.50	12.50	18.75
ADMINISTRATIVE	5.40	10.80	18.00	27.00
LOCAL TAXES	.72	1.44	2.40	3.60
ELECTRICITY, 25HP	33.50	33.50	33.50	33.50
STEAM GENERATION FUEL	9.00	18.00	30.00	45.00
TOTAL EXPENSE =	60.92	88.34	124.90	170.60
"GROSS REVENUE	-24.92	-16.34	-.90	9.40
WORKOVER @ \$20,000.00	21.45	21.45	21.45	21.45
DEBT SERVICE	10.80	21.60	36.00	54.00
SUBTOTAL	-57.17	-59.39	-58.35	-66.05

TABLE 6

ALASKAN NORTH SLOPE	\$/B
PRICE FOB USGC	16.00
OCEAN FREIGHT	<3.50>
PIPELINE COST	<4.25>
ROYALTY, 12.5%	1.03 (1)
STATE SEVERANCE	0.41 (1)
GROSS REVENUE	6.81
ADMINISTRATIVE	?
DEBT SERVICE	?
MAINTENANCE	?

NET REVENUE	-1.25 TO +2.00

1> CALCULATED ON WELL HEAD NET BACK

2> VERY ROUGH GUESSTIMATE

TABLE 8

SHUT IN PRODUCTION BY 12-31-87 @ \$16.00 BBL WTI

STATE	PRODUCTION KBBLS/D	PROBABLE LOSS %	SHUT IN KBBLS/D
TEXAS	2472	30	740
CALIFORNIA	1126	40	450
LOUISIANA	1408	20	280
OKLAHOMA	460	60	275
KANSAS	207	100	207
ILLINOIS	79	100	79
INDIANA	15	0	15
KENTUCKEY	21	100	21
MISSOURI	1	0	1
NEBRASKA	18	100	18
NEW YORK	2	100	
OHIO	42	100	42
TENNESSEE	3	100	3
PENNSYLVANIA	12	30	10
WEST VIRGINIA	10	100	10
OTHER			340
TOTALS			2440

Mr. STENHOLM. Thank you, Mr. Terrell.

Next is Mr. Gene Boone, executive director of the Boys Ranch, Abilene, TX. Gene, welcome.

TESTIMONY OF GENE BOONE, EXECUTIVE DIRECTOR, BOYS RANCH, ABILENE, TX

Mr. BOONE. Thank you, Mr. Chairman.

I did not really come today to make a statement. I came to learn a little something and see if I could find out what we need to do. But the more I have listened to this, especially the first two panels, it got me a little more concerned than I already was.

I am concerned about our natural resources, but I am also concerned about our human resources. And the programs that we have at the Boys Ranch depend on many in this room for the support of the program out there. And if they do not have the money and the dollars to help us, then that is going to cut significantly into our human resources that we have well down the road in the future.

Within the last 2 weeks, I was in San Antonio talking with administrators from all over Texas, Oklahoma, and New Mexico, and they are concerned about the trends that they see in the giving to charitable institutions. Whether you know it or not, 65 percent of all of the child care in the State of Texas is done in the private sector. We don't take any Federal money, and we take very little State money unless it is associated with an individual child. And there it only accounts for about 50 percent of the actual costs. So we come back to the people in the community to support the resources within the community to look after the care of youngsters that we take care of. And it concerns me very much that these producers and allied businesses are marginal in their profits because, as Mr. Darby said a while ago, people come around like the Boys Ranch, and the Boy Scouts, and the Girl Scouts. And that concerns me very much when every business has to look at cutting back in areas like that, where it has meant so much to the human resources in this country. It just concerns me very much.

Like I said, I did not come with a prepared statement but it concerns me very much, as you look at the ripple effect, that it is going to have not only on business—we are a small business, too, but our business is taking care of kids. And that is the future of this country.

Mr. STENHOLM. Thank you, Gene.

Next we will hear from E.L. Anders, Jr., a petroleum engineering consultant, Abilene, TX.

Dick.

TESTIMONY OF E.L. ANDERS, ABILENE, TX

Mr. ANDERS. I did not prepare anything. The only thing I wanted to do was—I had worked, as you probably know, in Caracas, Venezuela, Peru, Argentina, Spain, France, Iran, and Indonesia as consulting petroleum engineer.

Now, the main thing I noticed is that Glen Michel came up with a figure for operating cost, and lifting cost of \$13.50 to \$14.50 per barrel of oil. OK. Over in Iran, we were producing oil to the export

point for ± 12 cents a barrel. All the wells are flowing, there are no pumping units in the country. There are no water separators. Once a well produces over two-tenths of 1 percent water, they shut it in. A lot of those wells were producing 60,000 barrels a day. But Libya, most of the production there is flowing; the operating cost is very little. And I was consulting there for Mobil Oil and they had to move out because under their contracts to the Government they were losing money very rapidly.

We are competing with oil that is being produced for less than 20 cents a barrel, when it costs us \$13 to \$15 a barrel to lift it. And I think this is some fact that Congress ought to take into consideration. Because in Saudi Arabia, and Iran, they don't have to have pumping units or anything. They flow all their oil. And it costs them almost nothing. As the gentleman said, their labor is very, very cheap.

Thank you.

Mr. STENHOLM. Thank you, Mr. Anders.

Mr. Combest, any questions?

Mr. COMBEST. No; I really do not have any questions. But I do appreciate the facts you have brought to us and, of course, the additional concerns that we all have in the industry.

In visiting with you earlier, I had a chance to look over some of those figures. I think those figures are extremely beneficial in determining—taking a look at exactly what it is at various prices, with various size, various production wells, looking at in terms of what it is going to cost, and what amount of losses we have going into the—with current prices. And, again, you mentioned you were figuring those on \$16 a barrel. And we are talking in the neighborhood now of \$10, which we can probably project out exactly what those are going to be.

But one of the things we need that I think is extremely helpful is that when we have exact facts and figures that could be justified, that could be documented, it is pretty hard to argue with those; if someone talks about the fact that the industry is still making any money.

Mr. TERRELL. At the time that was done, I thought \$16 was a ridiculously low price. But just yesterday, I got a notice from my buyer that it had gone to \$13.75. But after I pay royalty, taxes, it's a little under \$10, I believe.

Mr. COMBEST. I don't have any questions, but, gentlemen, I appreciate your testimony.

Mr. STENHOLM. Dick, I have been saying that I thought the floor price for oil was going to be \$4, but after your testimony, I think the price could drop even lower than that.

Gene, I thank you for adding another dimension to the testimony today. We have not heard from any other witness today or yesterday with your perspective, and we appreciate your statement.

Mr. Terrell, I don't feel compelled to defend myself or Mr. Combest, but I would contest your statement that there are 3,000 lobbyists representing Saudi Arabia. I have never met one, and Mr. Combest has not either. The idea of \$100,000 or \$200,000 being offered to a Member of Congress by a foreigner is very much against the law. So if anybody is doing that, they are doing so at great personal risk within the confines of the law. Now, there may be one or

two Members of Congress serving in jail right now because of some past indiscretions, but such behavior is certainly not typical.

Member of Congress are not receiving contributions from foreign oil producers; this would be against the law. Period.

Mr. TERRELL. I realize that it is against the law. But I have heard the figures thrown around on several different occasions such as over 20,000 energy lobbyists in Washington, DC; and as many as 3,000 representing the Saudi Arabians. Now, whether that is an accurate figure or not, I do not know. I know that it has made me wonder, as well as a lot of other people wonder as to actually what is going on among the lobbyists in Washington, DC and why. I cannot understand why there would be that many up there anyway.

Mr. STENHOLM. Let me add that all lobbyists must be registered. In my 7 years in the Congress, I have never been contacted by any lobbyist representing the interests of foreign oil producers.

I just asked John Haugen of my staff if he had ever been contacted by a lobbyist representing a foreign oil producer. He has worked for former Congressman Omar Burleson, and did energy issues on my personal staff prior to his work on the subcommittee. In his 10 years on Capitol Hill, he has never had such a contact. The idea that there are 3,000 Saudi lobbyists doesn't seem very plausible and I would ask you for the record to check your facts and figures and advise us accordingly.

Thank you very much, Mr. Terrell.

We are now going to hear from Mr. Phil Kendrick, of Kendrick Oil Co.

TESTIMONY OF PHIL KENDRICK, KENDRICK OIL CO.

Mr. KENDRICK. Thank you, Congressman Stenholm and Congressman Combest. I did not come prepared to make a statement, but I just wanted to state that I think Mr. John Chalmers and Dr. Harrison and Glen Michel's views are not entirely the views of the rest of the oil industry in west central Texas, especially regarding an import fee.

I agree with all of the incentives suggested by Mr. Chalmers, some of which I think would be harder to attain than an import fee. And I certainly applaud all of them. I cannot think of one that I disagree with. However, some of the incentives that are put forward are worthless if we do not have a price that is profitable. His suggestion to double the ICD's every time we drill a well to encourage us to go explore for oil is worthless if we cannot have a price that makes it profitable. No one in his right mind is going to take a tax deduction just for the sake of a tax deduction. He has got to be looking at the possibility of making a profit as well as a tax deduction. However, I would be very happy to have a doubling of ICD's if our price makes it profitable. May I remind you that this does not enable us to avoid taxes, just to postpone taxes.

So I think the No. 1 question is: What can we do to make our business profitable? Right now, we are all losing money. And I will not go into all the horror stories. I think we have had sufficient testimony on that today; the facts are, we are all now losing money, and we cannot continue to lose money and stay in business.

And this is going to reverberate throughout the community, both in our banks, our retail stores, our real estate, and every other facet of our economy.

So the question is, what can we do? Now, several of them said that they were not for a quick fix. I want to tell you that I would love a quick fix, and the quicker the better.

We cannot prolong this fix for very long. We already are in great economic disarray in west central Texas, and I think it is going to reverberate throughout the Nation. And I think the consumers' windfall that they have had with the falling prices is going to also rebound against them at some point in time. Unfortunately, most of us will not be in the oil business when that happens and will not benefit from a price rebound. I am afraid that only our cash-rich internationals, such as Shell, British Petroleum, Exxon, the Saudi Arabians, Kuwaitis, and others, who have the cash to buy up oil and gas reserves at these very cheap prices look upon this as a great opportunity. They are the ones who will benefit from an eventual price rebound. I believe that the Saudi leaders are not a bunch of idiots like a lot of people think. I think they are very brilliant people, most of them educated right here in the State of Texas. They are petroleum engineers, economists, and they have Master's Degrees from Harvard. If they don't have it, they hire those that do. And when they decided to do what they did, it was not a rash move that they made, well, we will punish them for a few months and then we'll pop it back up, because I'm sure that they realized that would not accomplish what they had set out to do; and that was to reestablish their percentage of what they consider their fair share of the production. And it does not matter if oil goes to \$5 a barrel; it does not matter if it takes 5 years.

So I think we are looking at a long-term period of very low-priced oil. What are we going to do in the United States to protect ourselves from this political whatever you want to call it? It is political. It has nothing to do with the free enterprise system. It has to do with people trying to control the energy of the world. And they are doing it by knocking the price down, overproducing and knocking it down to a price that no one else can profitably stay in business, and, at the same time, saying, well, this is also a good opportunity to buy some reserves at a very cheap price. And if and when that day comes we get the price back up, we're in that much better control.

They have engineering firms in Dallas, they have engineering firms in Houston, in Midland, Oklahoma City. They are working with the banks. They know who is about to take bankruptcy. And they also are buying production as it becomes cheap. Exxon is now aggressively looking for production to buy; they have the cash to do it with. And a lot of the other majors also are cash rich. I am sure that British Petroleum is eyeing the North Sea very carefully.

I feel that right now we are in a position that we have to have something like an import fee. As much as I dislike an import fee, and other protectionist plans such as quotas, I believe an import fee is this Nation's only alternative. I am a conservative Republican, I have been for years. I may switch one of these days if things keep going like they are, just like Mr. Chalmers said. But I am not one of the liberals out here, way out in left field. I am one of the

conservatives of this district. And I think I speak for a lot of other conservatives when I say I think we must have an import fee.

The domestic oil producer pays taxes domestically. We are at a very unfair disadvantage with imported oil. We pay county taxes, we pay State taxes, we pay school taxes, we pay windfall profit taxes, we pay sales taxes, we pay sales taxes on goods and services, we pay Federal taxes. Imported oil comes in completely tax free.

Mr. Chalmers said he thinks that we ought to tax everything if we are going to tax oil coming in. I disagree with him on that one point. But, on the other hand, I am not too sure that oil is not the only imported commodity that doesn't have a tax on it. I think we are the only ones being left out. As I go down the list, I cannot think of a single item that does not have quota or a tariff or a fee or a subsidy of some sort. And oil has none of these.

Now, I think maybe we could call this a tax equalization fee to make imported oil and products bear at least the same taxes as our domestic oil. I understand there is a sliding scale import tax on oil now that ranges from 10 to 50 cents a barrel. But this doesn't compare to the amount of taxes our domestically produced oil is assessed.

As far as Canada and Mexico are concerned, they have guaranteed prices on gas and the amount of gas that they can bring into the United States, twice what we are getting here in west central Texas. And we have no guarantee that we can produce or sell a drop of gas the way contracts are being abrogated at the encouragement of our supposedly conservative FERC and our Energy Department.

So I would like to go on the record as saying I feel like I represent many, many oil and gas producers in west central Texas, and oilfield workers and secretaries that work for oil companies, and all other people that are affected peripherally in their jobs, in saying that I think an import fee is the most logical, the quickest, the best answer we can have. It would also help reduce the Federal deficit and we certainly would all be gaining from that point of view.

It is interesting that numerous people, the North Texas Oil and Gas Association, the East Texas Oil and Gas Association, the Texas Independent Producers and Royalty Owners Association, Governor Mark White, all the candidates for Governor are in favor of an import fee. I know former Governor Clements is for an import fee. And would you believe that even a Midwest Democrat from the Rust Belt named Lee Iacocco has stated that he thinks it's stupidity if we do not have a \$10 import fee oil and gas.

So I feel like I am in pretty good company, taking the stand I do. I am not way out in left field. I know there are some horrible things that can happen to you at anytime you propose anything in Congress. But I think it is time that we united all of the oil and gas operators, all the landowners, all of our consumers, all of our Congressmen in one united vote, and go for the quick fix and permanent fix. I think that we must have a stable price, one that we can depend on that we can operate under, and can make a profit and continue to produce all the wells, including the marginal wells. An import fee would give us a stable price to encourage us to go explore and maintain the reserves and the producing capability we

need. We have another reason that is more important than anything else. It is essential to our national defense to have a healthy domestic oil and gas industry.

Dairy products, lumber, asparagus, all these other things, peanuts are not necessarily essential to our national defense. They are all protected by import fees. Oil and gas is essential to our national defense. And also oil and gas and energy is the backbone to the economy of any industrialized nation. If you become dependent on foreign sources for the backbone of your economy, you are in deep trouble from an economic standpoint as well as a national defense standpoint.

Thank you very much.

Mr. STENHOLM. Thank you, Mr. Kendrick. Next, Ms. Susan Koerner.

TESTIMONY OF SUSAN KOERNER, INSURANCE AUDITOR

Ms. KOERNER. Thank you, Congressman Stenholm, Congressman Combest.

I did not come here intentionally to speak to the subcommittee. I did not even know it was going to be here today. I came in and checked into the Royal Inn last night. I am a working woman now. I am an auditor, insurance auditor and inspector. My husband and I bid on—and I emphasize—bid on Dynamite of Texas. We were explosive contractors for the State of Texas for predominantly the oil-field industry. When it started falling through and we were not able to get jobs there, we switched to utilities. And there is not much going on in construction either.

I have been in the past—I have cleaned hotel rooms, I have been a schoolbus driver, I have been a teacher's aide, I have been a telephone representative, and I prepared tax returns, and was a bookkeeper for 10 years. And my husband and I went into business in 1972 when he got out of the U.S. Army. He served 14 years. He was in Vietnam. He has an Army Commendation Medal; also has a letter of commendation from the Korean detachment that he was attached to.

We are little people, small people, a lot smaller than everybody else that has been testifying before this subcommittee. I think I consider ourselves placed on the backburner of America.

We are no longer in business, basically because of what Congress is doing to us. Not only that, it is also the insurance industry. We started out—you were talking about the bankruptcy laws. We have been very fortunate. We have not lost that much through bankruptcy for, you know, other people. Our gross income was \$240,000 a year, about \$20,000 a month. We were small. We could not afford to lose much money. I checked into all the people that we did business for trying to see that we did business for good people that were going to pay us. We have lost a total of \$3,600 in the 14 years we have been in business, \$600 to a nonbankruptcy person and \$3,000 to bankruptcy companies. We did have on the books 2 years ago a \$15,000 accounts receivable. We found out through the grapevine in talking to other people that this man had filed three bankruptcies in the past, was about to file bankruptcy again. I went and sat on his doorstep for 2 weeks to collect my money. I was the only

person that was able to get my money before he filed bankruptcy. And I don't know how great it was because we did happen to get our money, because I could not afford to lose \$15,000. That would mean I was going to lose my company.

This last summer, we started with the insurance problems, predominantly liability insurance. My liability insurance was \$7,000 a year. We have no liability claims in 14 years of business. My husband has been a safety officer in the Army. He belongs to the Society of Explosive Engineers; we both belong to it. We have all the OSHA training manuals. We stick to a safety program. We take all the precautions necessary not to have an accident. But yet my insurance was canceled. Last June, they canceled—they rewrote my insurance June 26; they canceled July 14.

Try in 1 month—try to get insurance, it was going to go from \$7,000 to \$32,000 for my insurance policy. I could not afford it. I only grossed \$240,000 a year. There was no way I could afford to program in that kind of price increase and still make any kind of money and get any kind of jobs that are possible.

I called CBS News in New York. I called the State insurance board in Austin. What I get from the State insurance board in Austin, that the solution is a liability pool like the workman's compensation pool. I don't think that is the problem. I think the insurance problem has been engineered in order to get the liability rates up. For what reason, I don't know; if they just want to make more money or if they are losing money. But the liability problem is engineered by the insurance companies in order to get their rates up and to make more money, not to take care of the little people that keep them in business or anything else.

I have no liability claims. Like I said, I went to the State insurance board. I finally called the president of the insurance company that I had the insurance with in Kansas City. He reinstated my insurance only through June 26, 1986, and he said find somebody else by then. So that gave me the ultimatum, I either had to find somebody else or go out of business by June 26, 1986. This was on August 15 that he told me this and reinstated my insurance. On August 19, because of the whole month of uncertainty over insurance problems, my husband had a stroke. We decided after that it wasn't worth it anymore.

We've tried. We're the little people down here on the bottom. We tried for 14 years to stay in business. I was tired of hitting my head against the wall and trying to make a go of it. Everything that we had done—we tried to stay in business, but the pressures are up above, up here. For what reason, I don't know. But it's not only—it's insurance, it is the bankruptcy laws. It is also—well, now it is oil and gas.

If you cut your arm out today, would you want a Band-Aid or a tourniquet?

I think this committee meeting here is a Band-Aid.

Since 1980, I have been writing you letters saying that I felt like the overall problem was a balanced budget. We still have not done anything in the last 6 with a balance of the budget. We are still sitting on the fence. We are still being mug-wasps. We've got our mug on one side and our wasp on the other, waiting for somebody else to do something. You're still sitting here having a committee

meeting, trying to decide what to do. In the meantime, while you are still trying to decide what to do, you are still chopping off businesses down on the bottom. You chopped off the lower level businesses. Just like Mr. Combest said earlier, he has been through a wide territory, a wide area, and he keeps losing small businesses that have been there 20 and 30 years. They are no longer there.

I am now working. I am an insurance auditor and building inspector. I do two jobs. Normally, you have one person doing insurance auditing and one person doing building inspections. I'm doing both jobs. I am also doing two territories trying to earn enough money to pay our household bills because my husband is no longer able to work. I have enough jobs through this week and the first of next week, and I have no more job offers after that. That's it, because I am an independent insurance auditor. Because of the turmoil in the insurance industry, the oil industry, the farmers and the ranchers; it is not just one. It is the whole United States is coming apart because you are trying to put Band-Aids on the problem and not fix the whole thing, and balance the budget and get down to the basics of what America is all about.

That's all. Thank you.

Mr. STENHOLM. Thank you, Ms. Koerner, very much for those comments.

Next, Mr. Oris Greever, vice president, Ballinger Butane Gas Co.

TESTIMONY OF ORIS GREEVER, VICE PRESIDENT, BALLINGER BUTANE GAS CO.

Mr. GREEVER. Thank you, Mr. Chairman, for this opportunity to appear before the committee here.

I am vice president, chairman of the board, and owner of Ballinger Butane Gas Co., a small LP gas and diesel fuel supply company in Ballinger, TX. Presently, I am serving on the board of directors of Texas LP Gas Association. So I feel like, to a degree, I am representing 15 other counties with about 21 codealers with similar problems. Of course, LP gas is an agribusiness, and oil-related also. The gentleman from Olney mentioning his REA bill, where they do not have REA, sometimes they use our fuel as a utility coming into play with the oil industry and agribusiness.

We have the same major problems that all these other people have outlaid before you today. The only other thing I would like to present and enter into the record is a new area, a new problem that hasn't been mentioned. Insurance has been.

With our business, we have a tremendous insurance problem that is going to affect not only us as business people, but our consuming public, which is a result of a 1980 Motor Carriers Act coming into existence, dictating that commencing January 1, 1985, dealers like myself would have a \$5 million liability policy as a requirement by the Department of Transportation, under section 30 of this act.

I thought that I would not have too severe a problem, possibly, because of my track record. I have owned the business for 15 years, purchasing a growing business that is operated under the same name now for, if we make it until next year, it will be 50 years. I have had an excellent track record insofar as insurance is con-

cerned. But this \$5 million has created quite a problem to us, not only cost, but availability.

My policy expired March 31, midnight. So I needed a new policy as of yesterday. At 3 in the afternoon, I finally obtained my \$5 million coverage, to be legal in order to operate the business. To give you some idea as to the impact of what this has on a small business, since it is fresh on my mind, in the 1984-85 fiscal year policy expiring April 1, the total premium was \$19,352 for my company. Yesterday, it was \$51,645, of which \$21,840 is the \$5 million umbrella coverage alone. And like I said, I had to beg, borrow, and plead to get it.

So I certainly would encourage you to assist us if you could in order to get some sort of relief whereby this coverage can either be lowered or some such thing for a cure.

So far, some of the feedback has been that this can be passed on to the consumers. These people, I think, can tell you they cannot stand any more being passed on to them. And up until 6 months ago, I did not know what bankruptcy really meant. We had been blessed in our business. But I now have a file which is growing each day with new people, new customers filing bankruptcy. So it is a problem.

I appreciate your hearing me. And I hope we can hear something in the future. Thank you.

Mr. STENHOLM. Thank you.

Mr. Combest.

Mr. COMBEST. Mr. Chairman, I really have no questions.

Pronounce your last name, please.

Ms. KOERNER. It's Koerner; the "o" is silent.

Mr. COMBEST. Koerner.

Ms. KOERNER. Yes, sir.

Mr. COMBEST. Ms. Koerner, I think that it is not only important, I think it is incumbent upon those of us who have the opportunity, and it is an opportunity even during extremely hard times, an opportunity to serve people. I think that is the greatest gift that an individual can be given.

I think it is very important in our efforts to be realistic, that we do not lose sight of the emotional concerns facing people. People are experiencing it in agriculture, they are experiencing it through small business, in the energy industry. They are looking at a loss and a change in a way of life that maybe they and the generations before them have known. They are looking at some very traumatic times. Your testimony was moving because that brings out the emotion that we have to be concerned about.

Speaking for myself, I think it is very easy a lot of times for people in an elected position to come back and say, "I'm going to make all this better. I've got all the answers. And it's going to be better tomorrow and next week." That may sound good. Tomorrow and next week is going to come and you are going to know it has not changed.

I think from a responsible standpoint, the position I have to take is that I want to deal with the problem as straightforward as I know how. I want to call it like I see it, and I want to have the input from people. I want to be able to be honest with them, know

exactly what the conditions are, and then let's get together and see if there is something we can do about those concerns.

That is what this is about. I can understand your concern that this is a Band-Aid approach to a problem that needs a tourniquet, or maybe needs a transfusion. But it is something that is available to us, something we try to do and, it is in all sincerity, to gather information which we can take and which we can say, "These are some of the problems we have in our districts. These are major concerns to us and something we want to do something about."

Again, no one needs defending. Charles Stenholm has got unquestionably the most dedicated record in the House of Representatives to balancing the budget of anyone I have ever seen. I continue to be amazed and my respect continues to grow because of his efforts in taking that commitment very, very seriously. I see it virtually daily in legislation that he is working on.

I think your concern is shared by a lot of other people. We feel like there are some major problems. We are going to do everything we can do to try to have an impact and see that some of these problems are addressed. I assure you, however, that we do understand the emotion that is involved in here and that this is not just a matter of dollars and cents; it is a matter many times, I think, of life blood.

I appreciate your comments.

Mr. STENHOLM. In spite of the nice things Larry said about me, I failed you and I have failed every other constituent in the 17th district in terms of doing what you asked me to do. And I accept that as a reality. I will continue to do the best we can admitting to you, as you have so eloquently told all of us today, that there are a lot of areas in which the Congress has failed.

I thank you for plugging in, as Larry says, the emotional side of the issue. Quite truthfully, I am getting a little more of this than I expected to hear, but that is the real world, and that is why we are here.

Phil, your statement is appreciated. Your disagreement with some of your fellow oil and gas producers is indicative of the problem that we have. And that is part of our system. Winston Churchill said democracy was the worst form of government ever created by man, save all the others.

Our system of government is imperfect. It does not work like a clock. We do not have ABC, here is what we do, and get massive agreement. There are no simple solutions. But your testimony points out that there are differences, and I happen to agree with you in regard to the oil import fee. We held a hearing of this subcommittee in Portsmouth, VA last fall, and butane dealers in Virginia were having the same problems with their insurance coverage. I don't know what the answer is, and I hope we don't end up making the situation worse. Federal intervention isn't always the answer, but sometimes it is unavoidable.

Thank you all for taking time to add your words.

I don't want to leave anybody out. If there is anyone else who wants to take a spot, we want to hear everyone that we can.

Mr. GREEVER. Mr. Chairman, may I make one other comment? Earlier on you mentioned your vocabulary—

My freshman year in college, I learned one big word, "Pithecanthropus erectus," which means erect man. Would you look after him tomorrow night and the extinct species down at the dam.

Mr. STENHOLM. Thank you.

Would you identify yourselves for the record?

**TESTIMONY OF JOHN SCOTT, PROPANE BUSINESSMAN,
SWEETWATER, TX**

Mr. SCOTT. I am John Scott, Sweetwater, TX.

I came to the subcommittee hearing because we have been in the propane business for several years. My dad has been associated since 1948, with an excellent track record of insurance. I had the \$5 million umbrella on everything last year. No problem. Couldn't get a bid until the night before. Got a bid about 4 in the afternoon. Had to send a check to Austin before they would even send me a policy. It went up from \$34,000 to \$61,000. I also have a killing problem with the DOT law requiring transports to have a \$5 million umbrella and exempting the one-man operation which has a single 3,500-water gallon capacity or less. I am the only one in my area that is under this law, and have nine dealers that are exempt, so my insurance is higher.

I am being penalized because my competitors are exempt. They do not have the \$61,000 expense. My insurance, if I only had Bob-tails of 3,500 water gallon or less, my operation would exempt me from the \$5 million coverage and the cost would be \$22,000 a year for insurance, which is approximately \$40,000 difference. It is pretty hard to compete if you have a \$40,000 expense that the others do not, besides the investment, to take care of your customers. I have grown and tried to get to where I can take care of my consumers, and I have tried to do what the major wants me to do. Like in the summertime, they will call me to pull propane, to help him out of a bind because of fullness. Then a lot of time in the wintertime we are requested to go 100 or 150 miles to get fuel, when the transports are not available. These consumers are going to be without fuel in the wintertime.

As the gas situation gets worse, we are seeing more plants where the liquid availability is getting smaller. And we are going to be requested to go further and have more storages. But the folks that have got into the business properly are not going to be able to stay with these extra costs.

To the accounts receivable problem, I am sitting here with several thousand dollars that are 90 days to 6 or 7 months old, tied in with FHA, because FHA requested all farmers turn in all their money so they can get their loans approved, and they would get money back. We still have FHA loans that have been approved, sitting in their offices with no where to go to get money. The bankers won't loan us money. The oil companies have cut us back to 10-day pay, electronic draft. We no longer can even write the check; they electronically draft our account. Believe it or not, they say gasoline is going up to the wholesaler. We have had a 7½-cent a gallon increase in the last 8 days at the refinery on diesel. I have had about a 4-cent increase on gasoline. In my hometown, I can go down

there and buy gasoline within a cent of a gallon of what I'm giving for it at the terminal in Midland, TX today.

You cannot pay these kinds of expenses for penny a gallon from rack to retail. Again, I have been getting notices that other companies are cutting their number of days down to 7 days pay from the day you pulled it. And we were in three terminals yesterday trying to get product. No product available. We got notification this morning that we are going on allocation of product. So I don't know what to do since we've got all these increases in costs and you can't get products, so you're going to have to travel further to get product. You can't get more margins. More of us are going to be gone, and I am talking about companies that have been around for a long time that have been very conservative, very economical, and do business as low a cost as you possibly can get by with.

That is all I have to say.

Mr. STENHOLM. John, let me make certain I understood what I thought I heard you say.

At a time when we're seeing a decline in oil prices to \$9.75, you have seen an increase in cost?

Mr. SCOTT. Yes, sir; that is right.

Mr. STENHOLM. You are about to go on allocation?

Mr. SCOTT. We are on allocation with American Petrofina—

Mr. STENHOLM. Why—

Mr. SCOTT. Refinery problems for the next 18 days, no product.

One thing, the refinery at Big Springs caught fire again Sunday, and burned part of the deal up, which has to do with it. But we will only get approximately 50,000 gallons for the first 15 days of the month.

Mr. STENHOLM. I think I know the answer to my own question. Our refineries, particularly our small independents, have taken a tremendous loss. As they buy this product, it takes about 60 days for it to go up to what they pay until they are able to charge you. Many of them took \$30, \$40 and \$50 million losses in that first month when the price changed. And so I think what I am hearing you say is that they are doing the only thing they can do to protect themselves now. Is that your interpretation?

Mr. SCOTT. It is my interpretation. We have received a comment, too, that if the price does not get back, there will be many terminations of product, there will not be product available. But my concern is that we are having rocks thrown at us because the oil prices are going down; my prices are going up. I am seeing these big boys come in and put us out of business, flat put the locals out of business because they could apparently buy this foreign price oil so cheap. Like say, today, rack to retail is 1 penny a gallon or less. And you cannot pay expenses with this margin—you know, in a town of Sweetwater's size, you might have a station there that is 12,000 gallons a month. At 1 penny a gallon, that is \$1,200.

Pollution insurance, they asked me for \$500 a station. Close to \$500 a month, for all stations, and I can't pay it. I am now filling out forms to send to Austin that list every tank we have owned ever, construction, and all this. The redtape is eating us alive.

Mr. STENHOLM. John, when you called me the other day on the phone and I asked you to come over and testify today, I thought we had pretty well covered all the problems. Now you have succeeded

right in the clean-up hitter to confuse me so much that I am not real sure that I know where I am going right now.

Mr. Combest.

Mr. COMBEST. I know I don't know where I'm coming from.

Mr. STENHOLM. But you have helped us consider another dimension of this problem. It is a very complex situation.

Mr. SCOTT. You know, we are being forced to cut off farm accounts because the bankers simply—with FDIC like they are, their regulations, they can't loan me money for past-due accounts. I have farm accounts that have been with me years and years and we are going to have to be the enemy. We have got to pay our bills while we are sitting here waiting for this FHA money. We were the nice guy. They came and talked to me; explained to me their situations, that the FHA said, "Look, turn this money in. We will get you going. We will get everything lined up." We tried to help them. Now they're all mad at me because I'm having to be the cut-off guy. And I just tried to work with them to get them over the hump.

Mr. STENHOLM. Hopefully, we are going to see some of these FHA problems solved very, very soon. Hopefully.

Mr. SCOTT. Well, thank you for your time, very much, sir.

Mr. STENHOLM. Thank you.

TESTIMONY OF WYNANT S. WILSON, ENGINEER AND GEOLOGIST, ABILENE, TX

Mr. WILSON. My name is Wynant Wilson. I am an engineer and geologist here in Abilene. And I would like to comment a little bit about what has been said.

As the price of gas and oil falls, many times the deliverability of a lot of these plants is decreased. So you are looking at a situation where he is getting his supply if he is—these natural gasoline plants. But if the price falls off, then the deliverability under many of these plants is going to fall. And then his product, therefore, is going to be in short supply. That is what he services. He cannot get to the Port of Houston or get to some import facility to get his product.

So up here in the hinterland, in other words away from a port facility, you are going to see what he is describing as an increase in price rather than a decrease in price.

Mr. STENHOLM. Thank you.

Please speak briefly, and then we are going to shut down; I'm sorry.

TESTIMONY OF J.M. PATTERSON, OIL BUSINESSMAN, EASTLAND- BRECKENRIDGE AREA, TX

Mr. PATTERSON. I just have a question.

I am J.M. Patterson in the Eastland-Breckenridge area. I am in the oil business.

It looks pretty gloomy for the small businessman in this area.

From your side of the table, on your subcommittee, you are taking your facts back. If anybody knows the facts, Congressman, you do. You have been in Odessa. You have made many trips out here. You know what the facts are.

What are your chances, our chances, of putting an import tax or not? And what is the timing? Can you expect any help out of the other Congressmen in the nonoil States?

Do you have any feel for that at all? That is my question.

Mr. STENHOLM. I would say that the chances of an oil import fee are very, very small at this moment, very small in implementing that in my opinion.

Mr. Combest.

Mr. COMBEST. I agree. There are other things that we are going to be looking at, other legislation that is in; repeal of windfall profit tax, relieving some of the tax burden—but, realistically, too, we do not want to hold out a lot of false hope. A lot of tax legislation and other bad legislation has not been considered this year.

One of the things that I think we have to remember in terms of reality, and I cannot give you any odds because it is hard to predict exactly what the House of Representatives is going to do, is that on a national economic basis there are a lot of people that see some positives from the price of oil dropping. They are seeing their costs go down. They are seeing an economic upturn. They are seeing some very good signs. Those people are going to have to be convinced that we have a serious—very, very serious—problem for them to be able to support something that could be perceived as a turnaround in the economic upswing.

Mr. PATTERSON. Let me relate this to you. Everybody here, I think, and most people, including yourself, are in the oil business. But first we are Americans. And so are the people that are not in oil-bearing States that are happy with the price turned down. But our major concern is for the future of our country.

Now, those people—the steel industry went through the same thing that the oil industry is going through now, 20 years ago. The automobile industry went through the same thing; also textiles. So this is not a new problem.

Mr. COMBEST. No; It certainly is not. And it is going to be a national policy, unquestionably, and that is how we are going to have to sell it.

Mr. PATTERSON. The Congressman brought up about the bumper sticker. Surely, the learned people in Congress are aware that 99 percent of the people that are in the oil business did not have bumper stickers on their cars. And that is just kind of a—I don't even like to enter into it.

Thank you for your time.

Mr. COMBEST. A lot of it is trying to share with them the problems that we are looking at in the future. That is what we will have to do in trying to sell this thing up there.

Mr. STENHOLM. Any closing statement, Mr. Combest?

Mr. COMBEST. Just to say again, Mr. Chairman, I appreciate the opportunity to be in Abilene and at the 2 days of these hearings. I commend you for holding them. The best we can do is to hope that we can get something done.

Thank you.

Mr. STENHOLM. Larry, I appreciate you taking time from your own schedule to come and be here in Abilene today and participate in this hearing. I appreciate your service on the subcommittee.

In concluding, let me thank everyone who has testified today. I think we have had an excellent hearing. I have learned something, too. I always learn something when I listen to the folks back home. And it is helpful in the education of myself. And I know that Larry agrees with that.

We thank all of you who have testified. We thank particularly the Abilene Chamber of Commerce, the West Texas Chamber of Commerce, and other organizations which have been helpful in putting together the panels today.

I thank everyone for the fine attendance we have had today. It shows the interest of the entire industry.

I want to thank Ms. Barbara Wall, the court reporter over here, who has faithfully listened to us 3 hours yesterday and 4 hours today. I thank Barbara for her work.

John Haugen, who many of you haven't met, is the fellow to my right. He is my staff director for this Small Business Subcommittee. He is the one who will be assembling this information for use as a reference tool during House consideration of legislation to address the current crisis within the oil and gas industry.

I thank everyone for being here. We will adjourn this hearing of our subcommittee.

[Whereupon, at 3 p.m., the subcommittee adjourned, to reconvene subject to call of the Chair.]

A P P E N D I X

PREPARED STATEMENT OF
MACK WALLACE, SENIOR MEMBER
RAILROAD COMMISSION OF TEXAS
BEFORE THE
UNITED STATES HOUSE OF REPRESENTATIVES
SMALL BUSINESS COMMITTEE
SUBCOMMITTEE ON ENERGY, ENVIRONMENT AND SAFETY ISSUES
AFFECTING SMALL BUSINESS
ABILENE, TEXAS
APRIL 2, 1986

Mr. Chairman, Members of the Committee:

My name is Mack Wallace. I am the senior member of the Railroad Commission of Texas, the state agency which, among other things, regulates the exploration and production of oil and gas and the transportation and sale of natural gas to the consumers of Texas.

America, because of pending devastation of its productive capability, is facing an energy crisis every bit as severe as that following the 1973 Arab oil embargo. I believe that this crisis can be avoided by imposing a tax on imported crude and refined petroleum products.

I

THE NATION'S ENERGY SECURITY IS IN GRAVE JEOPARDY

Let me begin by being blunt. An "energy war" is being waged and we are losing by default. In this time of crisis, we are stacking oil rigs faster than any peacetime army has ever stacked its rifles, faster than any navy has drydocked its fleet, or any air force has consigned its war planes to the boneyard.

Recent events of the past few days, weeks and months affecting this nation's energy position in the world should be cause for grave concern to all Americans, for we are witnessing an approaching tragedy with staggering consequences that threatens not only our economic stability but our national security as well.

These events impinge directly on the ability of the United States to search for and produce the natural resources that are absolutely essential to our national interest.

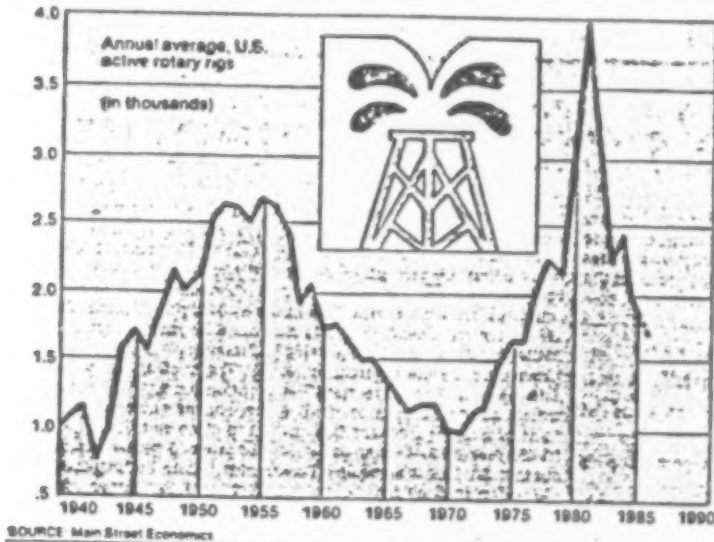
We must take swift action to extricate this nation's energy base from its current nose dive into subjugation under the direction of foreign governments.

II

DRILLING, JUST LIKE OIL PRICES, IS PLUMMETING

The jeopardy we face is dramatically illustrated by current drilling information. Drilling is acutely depressed and steel candidates for rig graveyards -- already heavily populated with

rusting derricks -- increase daily. History tells us that this level of activity leads inevitably to decline and dependency such as experienced in the 1970's.



Dallas Morning News 2/19/86

Let's look at the U.S. rig count, the leading barometer of industry activity and widely regarded as a measure of the oil and gas producing industry's health. The rig count in 1980-1981 averaged 4,000 active rotary rigs. At that level of activity, we added reserves equal to production and stabilized production. In contrast, consider 1975 when the average annual rig count was 1,650 rigs and our production was declining annually at a 4.5 percent rate. Oil prices were then in single digits (or slightly above) and appear headed that way again. See Attachment A.

Today, the U.S. rig count is under 1,250. That's down nearly 35 percent from as recent as December, 1985, when it was at 1,972. Active rigs appear to be headed for 3 digits, 999 or below, as crude prices continue to fall.^{*/}

Drilling has not reached these depressed levels since 1970 when, as you will recall, the Dow Jones bottomed at 584 in April. Following this severe period, reserves and production declined at alarming rates. The result was an intolerable dependence of this country on foreign energy supplies, as dramatized by the 1973 Arab Oil Embargo.

Our imports of crude oil and products are again creeping upward and presently amount to 5 million barrels a day, roughly 30 percent of our needs. Since 1972, the United States has spent \$549 billion for oil and oil product imports.

These numbers are unacceptable to me, especially at a time when our own government is also considering increasing taxes -- in the guise of tax reform -- on our energy explorers and producers.

^{*/}Another index of activity is drilling permits. A total of 11,818 permits were issued to drill for oil and gas in the United States during the months of January and February -- a decline of 21 percent from the comparable period in 1985. New field wildcat permits issued year to date number 1,035 -- down more than 32.5 percent from one year ago. Other exploratory permits -- drilling in and near existing fields -- total 1,197, a decline of more than 32.3 percent from 1985.

For Texas, the Railroad Commission processed 2,590 drilling permits in January, 1986, and 2,129 in February. The comparable figures for January and February, 1985, were 2,767 and 2,725, respectively. The February-to-February decline is about 22 percent.

America can, if it has the will, avoid increased dependency on uncertain foreign supplies. There is more oil and gas yet to be found and produced in America -- lots more with our improving technology -- but not under the present circumstances of foreign manipulation, coupled with the lack of a long-range national energy policy.

The predatory production and pricing tactics of Saudi Arabia and other foreign nations are directly responsible for the current drop in prices -- a price decline so severe that unless action is taken, our domestic production capability will be decimated within a short period. Once the damage is done, the Arabs will then feel free, in yo-yo like fashion, to back off their production and jerk prices up to prior levels.

To stabilize the current situation and to maintain the ability to produce at least two thirds of this country's supply of oil and liquids, the U.S. must maintain a price sufficient for reserve replacement in the U.S. The best mechanism for such essential support is a variable or sliding import fee on imported oil and products.

III

AT \$15 PER BARREL, AMERICAN PRODUCTION WILL DECLINE
SIGNIFICANTLY RESULTING IN INCREASED DEPENDENCY ON FOREIGN OIL

Let me put some numbers on the decline and dependency we can expect with oil prices at \$15 per barrel.

A. Immediate Impacts -- Many Stripper Wells Will Be Plugged

In the U.S. we have a large volume of production coming from wells with low daily yield. In Texas, a good representative of the U.S. Lower 48, more than 95 percent of all wells produce less than 50 barrels per day and two-thirds of all wells, the so-called stripper wells, produce 10 barrels a day or less. Specifically, in Texas, out of about 212,000 active oil wells, approximately 142,000 are stripper wells.

Obviously, production from these low-yield wells is very sensitive to price. In the U.S. a total of 1.3 million barrels per day is produced from about 450,000 stripper wells. About 400,000 barrels a day come from wells producing only three barrels per day or less. At \$15, many of these wells and a significant number of other more costly stripper wells, will be plugged and abandoned. In excess of 400,000 barrels a day of capacity could easily be lost over the next 12 months. If prices were to fall to \$10, the loss would probably be closer to a million barrels a day.

As a Railroad Commissioner charged with the responsibility of avoiding waste and conserving the state's oil and gas resources, I have a great concern about premature abandonments and plugging of wells which, at current pricing levels, are rapidly becoming uneconomic. Presently, our regulation, Statewide Rule 14(b) (2), requires

[plugging operations on each dry and inactive well (emphasis supplied) * * * be commenced within a period of 90 days after drilling or operations have ceased and shall proceed with due diligence until completed. For good cause, a reasonable extension of

time to start the plugging operators may be granted * * * [mainly for a non-polluting well for which the operator posts a bond].

We are presently examining this rule to see whether it fits today's producing environment. Well plugging is a costly step, averaging \$2 per foot or \$4,000 to \$5,000 for a well 2,000 feet deep; \$20,000 for a well 10,000 feet deep. Presently, the average cost of plugging wells which the operator has walked off and left and which the Railroad Commission then, as a last resort, plugs with state funds is about \$5,800 per well.

Plugs can be removed, and perhaps would be, if prices were to again dramatically reverse. However, the process of plug removal is also costly, ranging from \$500 to several thousand dollars per well depending on depth. Probably more important considerations than costs, however, are (a) the likelihood of mechanical damage to the well, particularly casing, in removing the 100 foot cement plug and/or (b) damage to the producing formation by cement used in the plugging process or, even more likely, water intrusion which impedes or precludes oil production. Expensive chemical treatment or "fracing" may partially rejuvenate formation-damaged wells. However, as a practical matter, many (if not most) stripper wells, once plugged, will never be returned to production. Furthermore, it's extremely unlikely that the economics would support drilling a new well to replace an abandoned stripper well. The net result, of course, is a loss of the reserves associated with any abandoned stripper well.

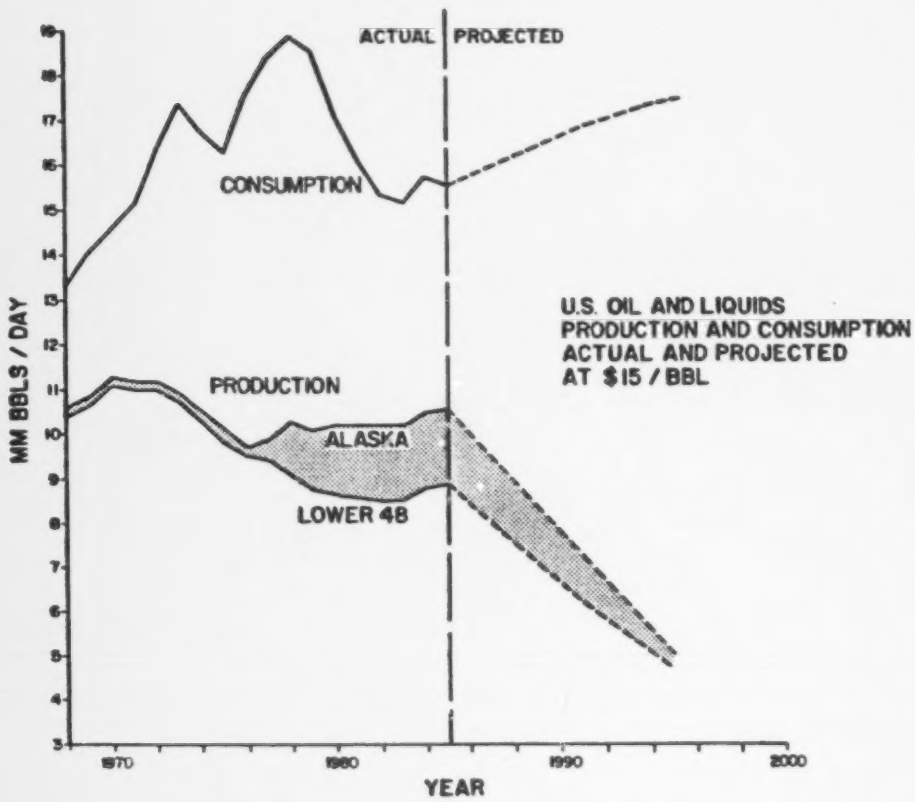
B. There Will Be Truly Devastating Impacts Later this Decade

Severely reduced cash flow at \$15 per barrel will reduce oil drilling drastically, both for reserve growth and new field discovery, yielding a corresponding loss of reserve additions. While additions nearly equalled production over the past five years, the reduction in drilling at a \$15 price will result in a Lower 48, non-stripper production decline of about 5% annually, essentially the decline level of the 1970's. This translates to a production loss of 1.6 million barrels per day by 1990, and nearly 3 million barrels per day by 1995.

Alaskan North Slope production, now 1.7 million barrels per day and chiefly from the Prudhoe Bay Field, will go into normal decline in 1987. An annual decline rate of between 12 and 15% is anticipated. This will reduce Alaskan North Slope production to about 1 million barrels per day by 1990, and to 600,000 barrels per day by 1995. While about 1 million barrels a day of additional capacity exists in already discovered, smaller fields on the North Slope, production and transportation costs will make this capacity uneconomical at \$15 per barrel, and little or no back-out of Prudhoe Bay decline is anticipated.

Lower oil prices will further depress natural gas prices with corresponding declines in drilling and production capacity. This decline will result in a loss of about 400,000 barrels per day of natural gas liquids production by 1990.

THE TOTAL PRODUCTION IMPACT BY 1990 WILL BE A LOSS OF ABOUT 3.1 MILLION BARRELS PER DAY OF LIQUIDS, OR ABOUT 30 PERCENT OF TOTAL PRODUCTION CAPACITY. If prices fall below \$15 per barrel,



or if lower prices persist beyond 1990, the loss of production capacity obviously will be greater.

IV

DEMAND FOR OIL WILL INCREASE AT A PRICE OF \$15 PER BARREL

U.S. consumption of oil and liquids has stabilized at about 15.5 million barrels per day over the past four years, after marked declines earlier. At \$15, increase in demand will be stimulated. By 1990, demand could be between 16.5 and 17.5 million barrels per day. EVEN AT A CONSERVATIVE GROWTH RATE, OUR PROJECTED 1990 IMPORT LEVEL WILL BE EQUAL TO THE HIGHEST LEVELS OF THE 1970'S. By 1995, we could be depending upon imports for two-thirds of our supply.

As the free world's largest producer and consumer of petroleum, we should not allow that to happen again.

V

OIL PRODUCTION IS A STRATEGIC PART OF OUR NATIONAL SECURITY

The ability of the United States -- all regions of the United States -- to provide a secure domestic energy resource base is a national issue and a strategic part of our national security.

We are all in this boat together. No purpose is served for one region of America to point to another and say, "Your end of the boat is sinking..."

I can assure you, when it comes to energy, we will sink or stay afloat together.

VI

THE SAUDI'S MANIPULATION IS SUCCEEDING;
AN IMPORT FEE SHOULD BE ADOPTED TO COMBAT THESE ACTIONS

News stories talk about the glut of world oil being "exacerbated" by OPEC. I would declare that the present situation is not "exacerbated" by OPEC, it is "caused" by OPEC.

Today's shattered oil market is nothing more than the calculated result of another determined effort by the Saudi Arabians to manipulate energy exploration, production, and price; as well as thwarting development of alternative energy sources.

They are succeeding. If this OPEC scheme is not challenged now, we shall be brought to our knees once again, as we were in 1973.

I urge you, in the strongest terms possible to respond swiftly to this challenge. We must not return control of our energy destiny to unstable foreign sources.

THE MOST IMPORTANT ACTION THIS COMMITTEE CAN TAKE IS TO RECOMMEND THE IMPOSITION OF A SLIDING TARIFF ON IMPORTED CRUDE OIL AND CRUDE OIL PRODUCTS TARGETED AT AN AGREED UPON PRICE.

Revenues generated would depend on the magnitude and level of the tariff.

Such revenues could be aimed at reducing this country's unconscionable deficit or, to further enhance energy security, the Strategic Petroleum Reserve could be increased.

In any case, the long-term, primary value of such a tariff on imported crude oil and products will be far reaching.

We will have stabilized America's ability to produce our natural resources. We will have declared to the world that we consider the exploration and production of our energy needs to be absolutely essential to our national security.

Members of this Committee, today, we find ourselves in common peril. If we are to survive, we must join in common purpose.

This nation must come together as one wheel with many spokes -- all determined to move the United States in the direction of energy production at home, which means jobs, self-reliance and national security.

For this reason, I urge this Administration and the Congress to enact as an emergency measure a "national security" tariff on crude oil and crude oil products imported into America. As I said earlier, this tariff could be a "sliding" tariff which would send a clear signal to oil producing countries that we are going to shore up our domestic capability and declare that we are prepared to protect our own reserves.

Let such a tariff become the cornerstone of a bipartisan domestic energy policy for which all can share in the responsibility.

VII

THE TIME TO ACT IS NOW

In this economic war for energy, I believe that if action is not taken now and Saudi Arabia or any other foreign government is permitted to continue to manipulate production levels and price, the first casualty in this world-wide scenario will be the United States followed by Britain's North Sea fields.

The control of energy, then, will be effectively placed for the foreseeable future in the hands of Persian Gulf producers and the West will have been dealt a crippling blow in its domestic ability to produce oil and gas. Consider these factors:

- Middle East and North Africa reserves of 433 billion barrels dwarf U.S. reserves of 27 billion barrels.
- 75 percent of the crude oil and products in the world is produced by governments -- not oil companies.

The production of oil and gas then becomes an instrument of foreign policy. This is clearly illustrated by the Soviet Union's decision of a few months ago to withhold the deliverability of crude oil to Western nations thereby raising the price of crude oil.

In times of danger, it has been this nation's history to rally its forces to fight for the values it considers essential to its survival.

Time and time again, the forces of the United States -- whether they be political, economic or military or from one

region or another -- have joined together to deflect strikes aimed at its cherished values.

One of the most basic of those values has been American independence. And, in our modern history, one of the ways we have successfully defended our independence has been through the recognition that a secure, domestic energy resource base is a strategic part of our national portfolio.

A national goal of energy independence that assures this country a long-term, adequate fuel supply has been a long-standing one -- up until now.

Isn't it time we take the necessary steps to free ourselves from this foreign dependence?

Isn't it time we free ourselves economically and free ourselves strategically?

Must we wait for an international disaster before we take the energy steps necessary for our own national interest and security?

* * * * *

Thank you.

ATTACHMENT "A"
 CONGRESSIONAL TESTIMONY BY
 COMMISSIONER MACK WALLACE
 4/2/86

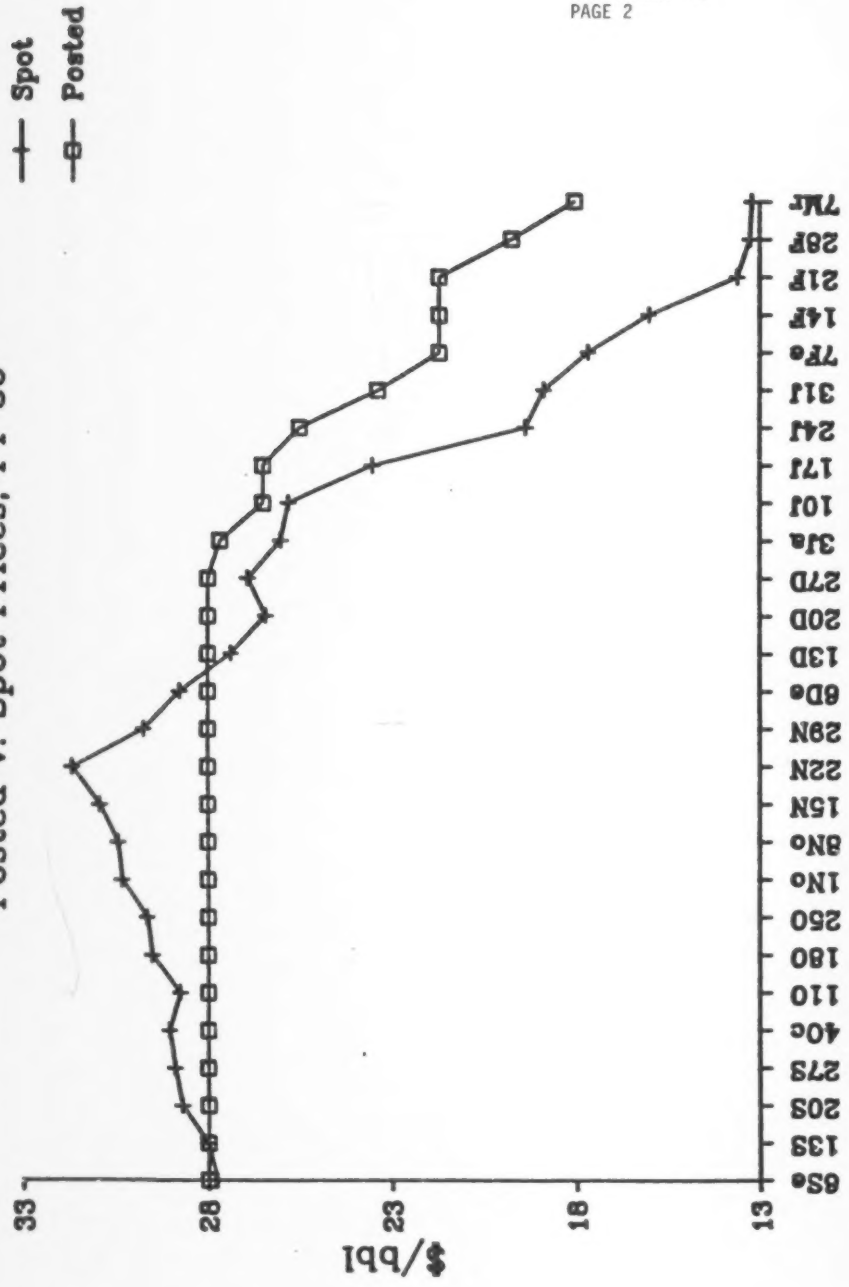
RAILROAD COMMISSION OF TEXAS
 Office of Research and Statistical Analysis

CRUDE OIL MARKET PRICES
 West Texas Intermediate (\$/barrel)
 March 13, 1986

	Price	Date	Year Ago
Spot oil market			
	14.00	3-12-86	28.10
	13.10	3-11-86	27.90
	12.85	3-10-86	27.90
Futures market (April delivery)			
	14.01	3-12-86	----
	13.10	3-11-86	----
	12.85	3-10-86	----
Contract (range of some recently announced offering prices)	\$14.00-18.75	3-12-86	28.00

Note: West Texas Intermediate prices have fallen by more than \$17 per barrel since late November, 1985, when the same barrel traded for \$31.85.

West Texas Intermediate Posted v. Spot Prices, FY 86



Austin American-Statesman Monday, March 10, 1986

Oil field 'undertaker' wishes business weren't so good

ODESSA (AP) — With oil prices plummeting, George Montgomery has one of the few thriving oil field businesses around.

"I'm the undertaker in the oil field. I plug wells, and there's a lot of that being done," said Montgomery, who owns Carr Well Service.

Montgomery said he is getting 15 to 20 inquiries about closing wells every day. In 1985, he was getting 1 or 2 calls a day.

"We're getting packages now," he said, pointing out that oil companies are closing several wells at once.

Some wells are "shut in" temporarily simply by turning a switch. But others, he said, are being plugged permanently with cement.

While well services companies have seen increased business in plugging wells, more traditional work of the past, such as well workovers, is being canceled.

"If they can't get their money out of it, they don't do it," he said.

Oil field operators calculate how long it will take to recover the cost of a workover before deciding to have it done and, at current oil prices, they often don't feel they can recover their money, said.

Montgomery hasn't added any employees to handle demand, but the well-plugging business increased "at least 100 percent" in the last three or four months. Montgomery said he expects the demand to continue for closing wells.

W.D. "Mooch" Bates, owner of Bates Well Service in Odessa, estimates his business is off about 30 percent from last year. But Bates took an optimistic view of the future. He said he hopes to see a gradual increase in oil prices and a recovery in oil-related businesses after April.

"It'll come back," he said. "When, that's the question."

Predictions are hard to make, he said, until he knows the results of a meeting this month of the Organization of Petroleum Exporting Countries.

The effects of the price decline, felt almost immediately by drilling companies, becomes more widespread as the rig count falls, Bates said.

"On every well that's drilled, you have 15 to 20 companies involved before it's on a pipeline," he said. Hughes Tool Co. reported the U.S. rig count last week at 1,248, compared to 2,011 a year ago.

M.J. Refiner, service manager of Odessa's Refiner's Rig Service, said business is slow and likely to remain so.

"I imagine we're in for quite a spell of it," he said.

Unemployment is increasing in the oil patch, Refiner said. "They have to put a prop under the oil price somewhere or Odessa's going to be a real disaster area."

Refiner said he is not certain drumming up business is a good strategy right now, because soon some customers could find themselves unable to pay for work they've had done.

"I don't know which way to jump," he said.